Speed
Environment
Price
Selection
Quality

THE SOUTHLAND CORPORATION

1995 ANNUAL REPORT

CONTENTS

Company Profile

The convenience retailing industry began in 1927 when a Southland Ice Company employee met the needs of his customers by selling bread, milk and eggs from the steps of his ice dock. The name 7-Eleven originated in 1946 when the stores were open from 7 a.m. until 11 p.m. Today, approximately 95 percent of all 7-Eleven stores in the United States and Canada are open 24 hours a day. With almost 15,400 convenience stores worldwide (see inside back cover for listing of stores by country and by state), 7-Eleven is the premier name in the convenience retailing industry and the largest operator, franchisor and licensor of convenience stores in the world.

IYG Holding Company (IYG) owns 64 percent of Southland's common stock. IYG is 51-percent owned by Ito-Yokado Co., Ltd., the fifth-largest retailer in the world, and 49-percent owned by Seven-Eleven Japan Co., Ltd., the longtime 7-Eleven licensee for Japan.

Southland's common stock is traded on The Nasdaq Stock Market under the ticker symbol SLCM.

Corporate Mission

The Southland Corporation exists to maximize the long-term market value of shareholder equity.

Our heritage is 7-Eleven. Its profitable growth and increasing dominance in convenience retailing will remain the core of our existence. We will be successful to the degree that we fulfill the needs of our customers. "What they want, when and where they want it" in a manner that provides added value, engenders loyalty and promotes a lasting relationship. To ensure Southland's continued excellence, we must retain the flexibility to anticipate opportunities and to master all forms of competitive challenge.

Our most important resource is people. Southland excels because of the quality, motivation and loyalty of every member of the Southland family. We are committed to innovation through participative involvement, and to fostering an environment of trust, respect and shared values.

As a responsible corporate citizen, Southland will conduct its business in an ethical manner with the highest integrity, while contributing to the quality of life in the communities it serves.

The ultimate measure of Southland's success is the optimal utilization of our collective resources and the perpetuation of a culture that is distinguished for its clarity of purpose, emphasis on individual responsibility and standards of excellence.

(Dollars in Millions, Except Per-Share Amounts)	1995	1994	1993	1992	1991
FOR THE YEAR:					
Net Sales	$ 6,745.8	$ 6,684.5	$ 6,744.3	$ 7,425.8	$ 8,009.5
Other Income (1)	71.0	66.4	61.6	57.9	54.4
Total Revenues (1)	6,816.8	6,750.9	6,805.9	7,483.7	8,063.9
Net Earnings (Loss) (2) (3)	270.8	92.0	71.2	(131.4)	82.5
Net Earnings (Loss) Per Common Share (2) (3)	0.65	0.22	0.17	(0.32)	0.24
Capital Expenditures	192.2	171.6	195.1	88.6	69.9
Interest Expense, Net (1) (3)	85.6	95.0	81.8	97.4	153.8
AT YEAR-END:					
Common Shares Outstanding (in thousands)	409,923	409,923	409,923	410,022	410,022
Number of Stores Operated or Franchised by Southland in U.S. and Canada	5,424	5,630	5,796	6,167	6,491
Number of Stores Operated by Licensees or Affiliates in U.S. and Overseas	9,961	9,067	8,360	7,593	6,995
Shareholders of Record (4)	3,097	3,060	3,130	3,373	3,314
Number of Employees (Full-time and Part-time)	30,523	30,417	32,406	35,646	42,616
Shareholders' Equity (Deficit) (3)	$ (880.8)	$ (1,157.2)	$ (1,248.4)	$ (1,318.8)	$ (1,210.3)
Book Value Per Common Share (3)	(2.15)	(2.82)	(3.05)	(3.22)	(2.95)
Total Assets	2,081.1	2,000.6	1,990.0	2,039.7	2,607.7

(1) Prior-year amounts have been reclassified to conform to current-year presentation.

(2) Net earnings (loss) for the years presented include the following:	1995	1994	1993	1992	1991
Loss on non-store assets sold (5)	—	—	$ (10.8)	$ (45.0)	—
Gain on debt restructuring	—	—	—	—	$ 156.8
Gain on debt redemption	$ 103.2	—	99.0	—	—
Tax benefit from recognition of net deferred tax assets	84.3	$ 30.0	—	—	—
Cumulative effect of accounting change for postemployment benefits	—	—	(16.5)	—	—
Severance and related costs	(13.4)	(7.4)	(7.2)	(17.5)	—
Gain/(Loss) on closings and dispositions of properties (5)	—	(3.7)	(48.2)	(44.3)	(14.4)

(3) The Company is required to prepare its financial statements since completing the 1991 Restructuring in accordance with Statement of Financial Accounting Standards No. 15 (SFAS No. 15). Under SFAS No. 15, the liability for the Company's restructured public debt as recorded on the balance sheet includes all future undiscounted cash payments, both principal and interest. For that reason, no interest expense will be recognized over the life of these securities, although the interest payments are tax deductible. The liability is reduced by the amount of the interest payments at the time they are disbursed. Those cash interest payments, which are paid semiannually, totaled $97 million during 1991, $65 million in 1992, $56 million in 1993, $35 million in 1994 and $35 million in 1995. In November, 1995, a portion of the restructured public debt was refinanced, thus reducing the restructured public debt's cash interest payments to $22 million annually beginning in 1996 through 2002, after which payments will decline because of bond maturities.

(4) The common stock began trading publicly on March 5, 1991, when the Company emerged from a voluntary bankruptcy reorganization.

(5) Includes completed closings and dispositions, as well as losses expected in the near future.

1995 was the fourth year of our long-term plan to revitalize 7-Eleven while setting the stage for sustained, profitable growth. To confront that challenge, we are "living in the basics" and focused on changing core processes to improve our ability to compete.

Our track record continues to reflect the progress we're making. Last year's fourth quarter marked 7-Eleven's eighth consecutive period of positive domestic same-store merchandise sales growth and the 12th straight quarter of higher merchandise gross profits per store. These results, despite sluggish economic conditions in Southern California where 18% of U.S. 7-Eleven stores are located, underscore how geographic breadth in some of the country's best markets has always been a powerful competitive advantage that allows us to weather regional economic cycles.

Transitioning to Growth.

We're pleased with our progress, but much remains to be done, and we are on the brink of an important transition. In 1996, while we continue reshaping core processes that are critical to our future, we also expect to begin to focus on developing new stores for the first time in nine years. As a result, our store base should be flat in 1996, versus the steady declines of previous years, and beginning next year, a significant number of new stores will be added on a net basis. Our objective is to ensure that each market has the critical mass necessary to support the "new 7-Eleven," including fresh-food production and combined distribution efficiencies, cooperative, mutually beneficial supplier relationships and effective advertising.

Over the last eight years, we have pruned more than 2,500 stores from our system, including those divested as a result of the 1987 leveraged buyout. At the same time, we have invested the majority of our capital in remodeling stores from coast to coast, the most extensive such effort in our history. We will complete that project this year, though we expect to continually "refresh and refurbish" stores going forward. However, our capital investment focus will shift decidedly to new-store development by 1997.

Our ability to build new stores and accelerate the implementation of other strategic initiatives is partly due to the successful refinancing of a portion of Southland's long-term debt, which freed substantial cash flow by eliminating sinking-fund requirements. We are especially grateful to our majority owners, whose additional investment further underscored their confidence in 7-Eleven.

With so many changes under way in core business processes, let me recap how some of 7-Eleven's most important strategies contribute to our long-term, customer-focused goals — speedy transactions, a reliable selection of quality products and services at fair prices and clean, safe and friendly stores.

Better Pricing.

Negative public perceptions about convenience-store pricing took a long time to develop and we won't change them overnight. Our goal is to deliver the competitive prices customers are demanding, without sacrificing margin. In the past, we relied on volume deals and promotional gimmicks to drive lower prices — temporarily. These were short-term solutions. They led to inconsistent pricing that confused our customers and actually reinforced traditional high-price perceptions. Valuable floor-selling space was used inefficiently to accommodate volume purchases at low costs. Constantly fluctuating order volumes increased production and storage costs for producers.

Today, we are seeking longer-term, sustainable solutions by asking our suppliers to help us rethink traditional pricing assumptions and practices and develop new approaches that meet both our needs. To some extent, these may include opportunities for global sourcing and lower product costs as the growing demands of almost 15,400 7-Eleven stores worldwide are matched with manufacturers' objectives.

The Power of New Products.

Strategic alliances with suppliers will be equally important to developing a constant stream of exciting new products for 7-Eleven stores. Last year's introduction of prepaid phone cards is a great example of how 7-Eleven's extensive store network can enable rapid and broad visibility for popular new products. By summer 7-Eleven was the nation's largest phone-card retailer, with consumer demand expected to continue growing swiftly. Similar development efforts are under way with suppliers of many other new products and services.

Quality Fresh Food Delivered Daily.

Changing demographics and lifestyles are driving busy consumers to seek new fresh-food options for themselves and their families. At 7-Eleven, we believe that customers shouldn't have to trade selection, quality or freshness for convenience. So as a beginning, 825 stores are receiving daily deliveries of fresh-made sandwiches, salads, bakery products and other perishable items, thanks to strategic alliances with food production and distribution specialists who develop and operate their own facilities in each

market. By year-end 1996, daily-delivered fresh food should be available in nearly half of our stores, and meanwhile we are developing and testing a number of delicious new items such as hot dinner entrees.

Daily store deliveries include items fresh-made exclusively for 7-Eleven from "World Ovens" bakeries and "Deli Central" commissaries. Many products have coded one- or two-day shelf lives and are labeled with the time and date they were produced. Together with bulk deliveries of perishable items from other vendors, these items are consolidated and sorted for daily delivery by store at state-of-the-art, cross-dock facilities called "combined distribution centers" or "CDCs." By eliminating costly by-store sorting and delivery chores, CDCs reduce vendors expenses dramatically. Over time, the resulting lower product cost to 7-Eleven will allow stores to offer customers a greatly improved selection of high-quality fresh food at more competitive prices.

Making this concept work in each market requires a revolutionary restructuring of traditional business relationships between Southland and its existing and potential vendors and distributors. That takes time, trust and economics that persuade each party of the long-term benefit to its business. Systemwide, it is essential that store staffs understand and master item-by-item management of fresh food, to maximize sales of popular items and minimize expensive product write-offs.

In a world oriented to immediate results, it's interesting to draw some perspective from the experience of one of our parent companies, Seven-Eleven Japan, which designed a daily-delivered fresh-food program in the 1980s for its customers. As the program developed and expanded deliveries to as many as three times a day in some stores, fresh food has grown as a percentage of sales to over 29 percent today. We believe similar long-term potential exists in our own approach and we look forward to updating you on our progress.

Automation.

Among the most important strategies we have under way today is installation of a systemwide retail automation network that will be unique to 7-Eleven. Unlike any other in the U.S. convenience-store industry, ultimately that system will be the "glue" that links all of 7-Eleven's new business initiatives because it will connect each 7-Eleven store to our accounting centers, corporate headquarters, fresh-food production facilities, CDCs, warehoused-grocery distributors and other vendors. It will not replace human thinking and judgment. Rather, it is technology that will provide stores with information and tools that lead to better ordering and merchandising decisions and ultimately improve 7-Eleven's competitive position.

Less than five years ago, the most current store data available to us was at least five days old. In addition, reports told us only what items each store had "purchased," but nothing about what was actually "selling." In contrast, the "new 7-Eleven" retail automation system will provide more accurate, timely information about precisely what 7-Eleven is selling, area by area, day by day, store by store and item by item — data formerly collected only by various suppliers who serviced each store. We will also be reclaiming our responsibility as retailers to use that data to improve the performance and customer focus of each store.

We believe that, better than anyone else, store managers, franchisees and their employees know their customers and the unique things that set their store apart. With retail automation, we intend to put them back in charge of their stores with tools that can help them make the most of those 2,000 square feet of selling space. Installing the system in phases enables us to automate processes that speed results and drive costs out of the system today. Phase one, scheduled to be completed in the first half of this year, involves the installation of backroom computers and automates many administrative tasks, thereby freeing store operators for more customer-focused services. Work recently began on the second phase and is designed to provide support for the number one job under "retailer initiative" — the ordering function.

A Consistent Vision.

Consistency is critical to 7-Eleven's credibility and progress as we continue this course. Over the last four years we have never wavered from our goal to deliver top-notch convenience to 7-Eleven customers — through a better variety of higher-quality products delivered faster, more efficiently and at better prices to stores that are clean and safe and provide fast, friendly service. We are encouraged by our progress to date and continue to believe that our choice of long-term, substantive change over cosmetic quick fixes will lead to profitable growth that will sustain 7-Eleven through decades of change to come.

Clark Matthews

Clark J. Matthews, II
President and Chief Executive Officer

March 22, 1996

The future taking shape at 7-Eleven today goes well beyond merely cosmetic changes. Instead, the new 7-Eleven involves customer-focused, proprietary processes designed to drive sustainable, profitable sales over the long term.

Improved ordering and merchandising are at the core of those processes, beginning with item-by-item management of each store. Infrastructure is being laid and training is under way today to provide store operators and their staffs with sales-tracking and forecasting tools to order precisely what their customers want to buy. For example, customers expect stores to be in stock on fast-moving merchandise, and last year 7-Eleven stores reduced out-of-stock occurrences significantly. In addition, slower-moving items are continuously deleted from inventory, and an average of 25 high-potential new items are made available to stores weekly. Domestic same-store merchandise sales responded with growth of 2.0 percent in 1995, and merchandise gross profits per store were up 3.1 percent.

"Team merchandising" is essential to maintaining an aggressive pace of new-item introduction at 7-Eleven stores. Groups of 7-Eleven merchandisers and suppliers combine ideas, talents and resources to create new products exclusively for 7-Eleven customers. New fresh-food offerings from "Deli Central" commissaries are a good example. Last year, "signature" lines of fresh-made products were developed, including gourmet sandwiches and salads, three varieties of rice bowls, new options for breakfast-to-go and a soon-to-be-launched test of tempting entrees in Texas. "World Ovens" bakeries have also rolled out a steady stream of fresh-baked new products, such as brownies, gourmet cookies and nearly 20 varieties of pastries, muffins (including low-fat), fresh New-York-style bagels and seasonal items.

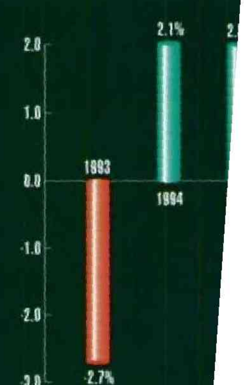
The operators of "Deli Central" commissaries, "World Ovens" bakeries and combined distribution centers are 7-Eleven's strategic partners in market-by-market fresh-food networks. As third-party specialists, they own and operate these facilities, working closely with 7-Eleven to develop and deliver the freshest, quality food at the lowest possible costs exclusively to stores throughout each market. In 1995, 825 7-Eleven stores in the Texas, Philadelphia, northern New Jersey and Long Island markets featured daily-delivered fresh food. Plans for 1996 will add the program to another 1,400 stores in the Denver/Colorado Springs, Orlando/Tampa, Richmond/Norfolk, Baltimore, San Jose and Chicago markets.

Offering a wide array of convenient financial services and products like ATMs, money orders, copiers, fax machines and lottery ticket sales, is another example of 7-Eleven focusing on the needs of its customers. In 1995, 7-Eleven introduced and practically overnight became the nation's largest retailer of prepaid phone cards. The market for this product has taken off rapidly and has tremendous long-term potential, underscoring the importance to 7-Eleven of being on the leading edge of new-product development and introduction.

By year-end, a vast majority of 7-Eleven retail gasoline facilities will meet 1998 EPA requirements due to comprehensive upgrades both above and below ground. Remodeling at most of the 1,978 stores offering retail

new merchandise processes and techniques, store operators and their sales associates now forecast orders for precisely what they believe their customers want to buy. Those orders include new products like daily-delivered fresh food, which should be available in more than 2,200 7-Eleven stores nationwide by year end 1996.

Same Store Merchandise Sales Growth



Merchandisin

gasoline includes brighter lighting, new dispensers and canopies, as well as pay-at-the-pump capability at 1,000 facilities by the end of 1996.

Breakthrough thinking about distribution of direct-store-delivered items is fueling 7-Eleven's ability to deliver on higher standards of freshness, selection, quality and value. Combined distribution centers (CDCs) are the vanguard of that new, more customer-focused approach.

CDCs enable 7-Eleven stores to get daily deliveries of fresh food while reducing costs for both 7-Eleven and the suppliers who use them. Once a day, suppliers deliver the consolidated orders from all stores in a market to the local CDC in only one stop. This approach spares them the high cost of sorting and delivering orders to as many as 250 separate locations. Each CDC is a state-of-the-art, cross-dock facility that then "combines" products ordered by 7-Eleven store staff from multiple vendors, for daily delivery to each store during predawn hours that are least disruptive to customer parking and shopping, as well as store operations.

Daily deliveries ensure customers unprecedented freshness and value in the products they buy at 7-Eleven, from fresh-made sandwiches, salads, and pastries to milk, fresh fruit, bread and packaged bakery goods. Daily delivery also makes 7-Eleven a more attractive customer to vendors to whom guaranteed product freshness and cost-effective distribution are important.

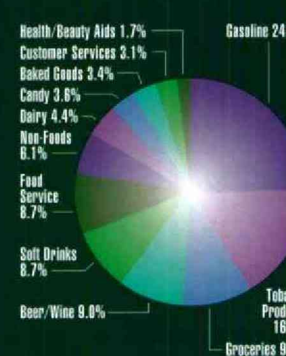
Most of all, CDCs support 7-Eleven's belief in the importance of "retailer initiative." Under this premise, the "new 7-Eleven" returns to individual store operators both the right and responsibility to order and stock merchandise they know their customers will want. Ordering through CDCs enables them to depend on delivery dates and times, offer a better selection of fresher products at competitive prices and stay in-stock, especially on fast-selling items. So "retailer initiative" simply underscores the ability of store operators to provide better, faster and more value-based service to 7-Eleven customers.

The ability of CDCs to enhance 7-Eleven customer service was particularly evident during the "Blizzard of '96," which crippled much of the Northeast for several days in January. Facing road conditions that severely limited transportation, suppliers were forced to limit deliveries to only their largest customers, including area CDCs. As a result, 7-Eleven stores remained well-stocked at a time when customers needed them most, while many competitors experienced product shortages and empty shelves.

In 1995, CDC development teams built on learnings from the initial facilities to develop business models for the remaining major 7-Eleven markets. As part of that process, potential strategic partners were identified and evaluated for several areas. As a result, CDCs are scheduled to open during the first half of 1996 in Denver and Colorado Springs, Colorado; Baltimore, Maryland; San Jose, California; Orlando and Tampa, Florida; Richmond and Norfolk, Virginia; and Long Island, New York, where an expanded facility will replace the current test operation.

Combined distribution centers, owned and operated by third-party experts, enable 7-Eleven to offer customers a wide selection of high-quality fresh food at competitive prices. In addition, daily deliveries help to ensure that stores have the freshest products available and remain in-stock on fast-selling items.

Southland Convenience Store Sales by Category



Distribution

Another important link in 7-Eleven's distribution system is McLane Company, Inc. McLane delivers warehoused-grocery items to 7-Eleven stores through a nationwide network of 10 distribution centers, as well as 15 smaller rapid-response centers that enable stores to replenish high-demand items promptly. McLane, the country's largest convenience-store distributor, has worked closely with 7-Eleven to improve key delivery performance measures. As a result, McLane's fill rate on 7-Eleven store orders was over 99 percent last year, and 98 percent of deliveries were made on time. In addition, McLane will soon be among the first suppliers to integrate its ordering processes with 7-Eleven's retail automation system.

Magazine distribution is yet another example of how 7-Eleven is revamping processes to deliver customers a "fresher" product. Traditionally, convenience stores are among the last retailers to receive newly published magazines, mainly due to volume and distribution-cost issues. About 70 percent of publication sales occur within the first 72 hours after release. More than 5 million customers shop every day in 5,000 stores nationwide, underscoring the potential sales impact of "fresher" magazine availability. With that in mind, 7-Eleven's magazine distribution process is being restructured to reduce the number of suppliers and product cost, and provide 7-Eleven customers access to new issues hot off the presses.

Retail automation is also critical to 7-Eleven's future ability to develop and deliver to customers an expanding selection of reasonably priced, high-quality, fresh-made products. By facilitating communication among stores, suppliers, distributors and headquarters offices, 7-Eleven's proprietary system will build efficiencies into ordering, distribution and merchandising processes that result in improved product cost and quality for customers. As a result, the system is much more than a scanning device and will exceed the features of any off-the-shelf software that exists today in the U.S.

By creating its own system, 7-Eleven takes charge of critical merchandising data that used to reside with the suppliers who gathered it to increase their own sales. With storewide data captured and organized through the new system, store operators will have more timely, accurate, item-by-item data to use in making better-informed ordering and merchandising decisions in their stores. People on the front lines of each store are in the best position to order accurately based on their knowledge of area weather forecasts, competitive activity and local events that may affect store traffic. Retail automation is intended to supplement that important base of knowledge by providing tools that help make each retailer more effective.

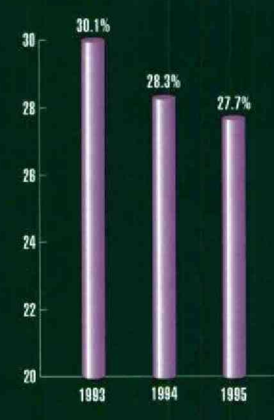
Begun in 1994, development of this system will be a four-year process. By implementing the system in phases instead of waiting years for the final product, many manual processes in the stores are being automated today. That sets the stage for time and expense savings that drive costs out of the 7-Eleven system and ultimately will free store operators to invest more time in customer-focused activities.

Installation of the first phase, scheduled to be completed in early 1996, will create the base for a company-wide electronic network, help process store-level administrative reports and provide the store operator with

Automation

A proprietary retail automation system is now being installed in 7-Elevens nationwide that will link each store with suppliers, distributors and corporate offices. By making the ordering, distribution and merchandising processes more efficient, store operators will be able to spend less time on administrative tasks and more time on customer-focused tasks.

Operating, Selling, General and Administrative Expenses as a Percent of Sales



more accurate and timely information. Phase two is designed to provide support for the number one job of the store operator — ordering. In addition to a central item master database, new hand-held devices will help enhance and support the product ordering decision and receiving processes by calculating product movement and "scanning-in" deliveries.

Directing more resources to the stores has required belt-tightening and greater efficiencies in every part of the 7-Eleven system. Among other things, we have reduced the ratio of operating, selling, general and administrative expenses to sales for the last three consecutive years. Employee and franchisee support is integral to the success of changes in every aspect of 7-Eleven operations. Their input, ideas and participation are being sought much earlier and more frequently than in the past. In addition, weekly video teleconferences that link 7-Eleven division operations across the country and weekly meetings between store operators and field consultants have helped ensure more consistent messages and strategies amidst the fastest-paced change in 7-Eleven's history.

As new, customer-focused initiatives such as pricing, daily-delivered fresh food and retail automation continue taking shape, 7-Eleven is ready to begin growing again.

This year, new-store development will resume for the first time in nine years, thanks in part to the successful refinancing last November of a portion of the company's long-term debt. Though unit growth is expected to be flat in 1996, significantly more new stores will be added on a net basis each year beginning in 1997. Those new units in each market will expand the critical mass and efficiencies of the fresh-food commissaries, bakeries and CDCs that are so important to the future of 7-Eleven's daily-delivered fresh-food program.

Over the last eight years, more than 2,500 stores have been sold or closed as 7-Eleven consolidated its presence in some of the country's strongest and most promising markets. Now over 5,400 stores strong in the U.S. and Canada, 7-Eleven remains the country's largest convenience retailer and, by year-end 1996, will conclude a four-year remodeling program, the most extensive in its history. In addition to the brighter, better-organized look of the "new 7-Eleven," security systems will have been installed in stores nationwide by the end of March this year, including 24-hour closed-circuit video cameras, with monitoring capabilities and alarm-activating devices. These new systems underscore 7-Eleven's long-time leadership in store-related crime-prevention issues and have elicited positive feedback from customers and store personnel, as well as media and law enforcement officials.

Customer response is translating to higher and more profitable sales in 7-Eleven markets where stores have been remodeled and daily-delivered fresh food implemented. Women shoppers, normally not common convenience-store patrons, are visiting the stores in noticeably greater numbers, and overall shopping frequency and transaction size have increased as well. By the end of this year, the momentum of the "new 7-Eleven" will accelerate rapidly with stores remodeled in every market, daily-delivered fresh food available in nearly half, store closings substantially complete and aggressive new-store development under way.

After years of store divestitures and pruning, as well as the extensive remodeling of the remaining store base, 7-Eleven is once again ready to increase its presence in existing markets. Later this year, 7-Eleven will start the process of developing sites and by 1997 will begin adding a significant number of new stores each year.

Growth

(Dollars in Millions, Except Per-Share Data)	Years Ended December 31 1995	1994	1993	1992	1991
Net sales	$ 6,745.8	$ 6,684.5	$ 6,744.3	$ 7,425.8	$ 8,009.5
Other income (a)	71.0	66.4	61.6	57.9	54.4
Total revenues (a)	6,816.8	6,750.9	6,805.9	7,483.7	8,063.9
LIFO charge (credit)	2.6	3.0	(8.7)	1.5	(7.2)
Depreciation and amortization	166.4	162.7	154.4	180.3	200.1
Interest expense, net (a) (b)	85.6	95.0	81.8	97.4	153.8
Earnings (loss) before income taxes, extraordinary items and cumulative effect of accounting changes	101.5	73.5	(2.6)	(119.9)(c)	(66.3)
Income taxes (benefit)	(66.1)(d)	(18.5)(e)	8.7	11.5	8.0
Earnings (loss) before extraordinary items and cumulative effect of accounting changes	167.6	92.0	(11.3)	(131.4)	(74.3)
Net earnings (loss)	270.8(f)	92.0	71.2(g)	(131.4)	82.5(h)
Earnings (loss) per common share (primary and fully diluted):					
Before extraordinary items and cumulative effect of accounting changes	0.40	0.22	(0.03)	(0.32)	(0.22)
Net earnings (loss)	0.65	0.22	0.17	(0.32)	0.24
Total assets	2,081.1	2,000.6	1,990.0	2,039.7	2,607.7
Long-term debt, including current portion (b)	1,850.6	2,351.2	2,419.9	2,560.4	3,037.1

(a) Prior-year amounts have been reclassified to conform to current-year presentation.

(b) The Company's 1991 public debt issuances are accounted for in accordance with SFAS No. 15 as explained in Note 8 to the Consolidated Financial Statements.

(c) Loss before income taxes, extraordinary items and cumulative effect of accounting changes include a $45,000,000 loss on the sale and closing of the Company's distribution and food processing facilities.

(d) Income taxes (benefit) includes an $84,269,000 tax benefit from recognition of the remaining portion of the Company's net deferred tax assets as explained in Note 14 to the Consolidated Financial Statements.

(e) Income taxes (benefit) includes a $30,000,000 tax benefit from recognition of a portion of the Company's net deferred tax assets as explained in Note 14 to the Consolidated Financial Statements.

(f) Net earnings include an extraordinary gain of $103,169,000 on debt redemption as explained in Note 8 to the Consolidated Financial Statements.

(g) Net earnings include an extraordinary gain of $98,968,000 on debt redemption and a charge for the cumulative effect of an accounting change for postemployment benefits of $16,537,000 as explained in Notes 8 and 12 to the Consolidated Financial Statements, respectively.

(h) Net earnings include an extraordinary gain on debt restructuring of $156,824,000.

RESULTS OF OPERATIONS

Summary of Results of Operations

The Company's net earnings for 1995 were $270.8 million, compared to net earnings of $92.0 million in 1994 and $71.2 million in 1993. Continued improvement in the Company's operating performance resulted in a 38% increase in 1995 earnings before income taxes.

(Dollars in Millions, Except Per-Share Data)	Years Ended December 31 1995	1994	1993
Earnings (loss) before income taxes, extraordinary gain and cumulative effect of accounting change	$ 101.5	$ 73.5	$ (2.6)
Income tax benefit (expense)	66.1	18.5	(8.7)
Extraordinary gain from partial redemption of the Company's 4½ and 5% debentures in November 1995	103.2		
Extraordinary gain from redemption of the Company's 12% Senior Notes (refinanced in August 1993)			99.0
Cumulative effect of accounting change for postemployment benefits			(16.5)
Net earnings	$ 270.8	$ 92.0	$ 71.2
Net earnings per common share (primary and fully diluted)	$ .65	$ .22	$ .17

Each years' results included the following special or unusual items, in addition to the items noted above:

(Dollars in Millions)	Years Ended December 31 1995	1994	1993
Severance and related costs	$ (13.4)	$ (7.4)	$ (7.2)
Deferred income tax benefit	84.3	30.0	
Loss for store closings and dispositions of properties		(3.7)	(48.2)
Disposition of Citijet, a fixed-base operation at Dallas Love Field Airport			(10.8)

The Company's operating improvement in 1995 was primarily due to savings in "Operating, Selling, General and Administrative" (OSG&A) expenses. Although store closings (173 average) resulted in a decline in total merchandise gross profit compared to 1994, average per store merchandise sales and gross profits improved in each quarter in 1995 over 1994.

(Except where noted, all per-store numbers refer to an average of all stores rather than only stores open more than one year)

Financial Statement Changes

The Company has made the following changes to its financial statements for all years presented, and has restated such items in the comparisons provided to maintain consistency:

i) Total Revenues — interest income was reclassified from "Other Income" to "Interest Expense, Net". (See Note 1 of "Notes to Consolidated Financial Statements")

ii) Cost of Goods Sold (COGS) — Buying and occupancy expenses were reclassified to OSG&A expenses. Although these changes were made for financial statement purposes during the fourth quarter of 1995, prior Management's Discussion and Analysis had been excluding buying and occupancy expenses, as well as certain merchandise and gasoline inventory-related expenses, from per store gross profit and margin results.

iii) Profit Sharing Contribution — this expense is now included in OSG&A expenses.

Management Strategies

Since 1992, the Company has been committed to several key strategies that it believes, over the long term, will further differentiate it from its competitors and allow 7-Eleven to maintain its position as the premier convenience store chain in the industry. These strategies include: an upgraded store base; a customer-driven approach to product selection; an everyday-fair-pricing policy on all items; daily delivery of fresh perishable items; introduction of high-quality, ready-to-eat fresh foods; and the implementation of a retail automation system.

The Company plans to upgrade its store base by remodeling existing stores, closing underperforming stores and developing new sites. Over the last few years, the Company has devoted the majority of its capital resources toward the most extensive remodeling of its store base ever undertaken. In conjunction with the remodeling program, the Company has been pruning its store base by closing or disposing of those stores that are not expected to achieve an acceptable level of profitability in the future. As a result, the Company closed 228 stores in 1995, 184 in 1994 and 401 in 1993. The Company expects to complete its remodeling program by the end of this year; however, it will continue to refurbish its store base as necessary. The planning process for new store sites is well under way. The Company's capital investment focus will shift to

store development (see Liquidity and Capital Resources — Capital Expenditures). Initial plans are to strengthen its position by expanding the store base in existing markets, with store openings in 1996 expected to offset store closings/dispositions. However, by 1997 the Company expects new store openings to significantly outpace closures each year.

The customer-driven approach to merchandising, which was adopted by the Company in 1992, continues to focus on providing the customer an expanded selection of quality products at a good value. This is being accomplished by emphasizing the importance of ordering at the store level, removing slow-moving items and aggressively introducing new products in the early stages of their life cycle. This process, which has contributed to improved sales and profits, will be an ongoing part of managing our business in a continual effort to satisfy the ever-changing preferences of our customers.

The Company's everyday-fair-pricing strategy, which was introduced in 1992, has provided consistent prices on all items by reducing its reliance on discounting. As a result, some product prices were increased, while others were lowered to achieve more consistent pricing on all products. Going forward, the Company plans to migrate toward lower retail prices as lower product costs are achieved through contract negotiations or strategic alliances with suppliers and distributors.

Daily delivery of fresh perishable items and high-quality ready-to-eat foods is another key management strategy. Implementation of this strategy includes third-party development and operation of combined distribution centers ("CDC"), fresh-food commissaries and bakery facilities in most of the Company's markets around the country. The commissary and bakery ready-to-eat items, like fresh sandwiches and pastries, along with goods from multiple vendors such as dairy products, produce and other perishable goods, are "combined" at a distribution center and delivered daily to each store. In addition to providing fresher products and improving in-stock conditions from daily deliveries, the combined distribution is also intended to provide lower product costs, in part from vendors' savings, through this approach. The Company expects the improved freshness and lower cost of the products from these operations to improve sales and gross profits. At the end of 1995, over 800 stores were serviced by the CDC's and carried fresh food products manufactured by the commissaries. Further expansion of these programs is anticipated in 1996 in the following markets: Denver/Colorado Springs, Baltimore, Richmond/Norfolk, San Jose, Orlando/Tampa, and Chicago. When operational, CDC's in these markets will make daily-delivered fresh food available to nearly one half of the Company's stores.

The development of a retail automation system began in 1994. The initial phase, which will be completed in early 1996, involves installing in-store processors ("ISP") in each store that will automate accounting and other store-level tasks. The second phase involves installing cash registers which, among other things, will feed data directly to the ISP. After future phases are complete, the system will provide each store and its suppliers and distributors with on-line information to make better decisions in anticipating customer needs.

Sales

The Company recorded net sales of $6.75 billion for the year ended December 31, 1995, compared to sales of $6.68 billion in 1994 and $6.74 billion in 1993. To strengthen its store base (see Management Strategies), the Company has closed more than 800 underachieving stores over the last three years. Same store merchandise sales increases since 1993 have minimized the lost sales from store closings, resulting in total sales remaining flat during this time period. In addition, 1994 and 1993 merchandise sales results were adversely impacted by the deflationary effect of cigarette price reductions (on certain premium brands) associated with manufacturers' cost reductions starting in August, 1993. The total sales increase in 1995 was primarily due to higher gasoline gallons and retail sales price per gallon.

U.S. same-store merchandise sales increases or (decreases) as compared to the prior year and inflation information is presented below:

Increase/(decrease) from prior year	Years Ended December 31 1995	1994	1993
Same-store sales	2.0%	2.1%	(2.7)%
Same-store real growth; excluding inflation	—	2.8%	(4.7)%
7-Eleven inflation (deflation)	2.1%	(.7)%	2.2%

Overall, domestic same-store merchandise sales growth continued its positive trend in 1995, however, results varied by geographic region. The largest increases occurred in those areas with the highest percentage of completed remodels (Florida 4.8%, Texas/Colorado 4.1%). Conversely, the Southern California area, which includes 18% of the Company's domestic stores, experienced a decline of almost 1.5% due to a sluggish economy. In addition, this is the area where the lowest percentage of remodels has been completed.

Gasoline sales dollars per store increased 4.0%, 8.7% and 9.1% in 1995, 1994 and 1993, respectively. This improvement is primarily due to per store gallonage improvement of 1.0% in 1995, 7.8% in 1994 and 11.1% in 1993, reflecting

the impact of several successful business strategies. Gallon volumes in 1995 did not sustain the high growth levels experienced in 1993 and 1994 as a result of market factors which affect the way the Company manages its gasoline business.

Other Income

Other income of $71.0 million for 1995 was $4.6 million higher than 1994 and $9.4 million higher than 1993. The improvement is primarily the result of increased royalty income from licensed operations.

Gross Profits

Merchandise Gross Profit Data

	Years Ended December 31		
	1995	1994	1993
Merchandise gross profit — *dollars in millions*	$ 1,790.2	$ 1,791.1	$ 1,847.9
Increase/(decrease) from prior year			
Average per store gross profit dollar change	3.1%	1.7%	2.4%
Margin percentage point change	(.01)	(.50)	1.21
Average per store merchandise sales	3.1%	3.2%	(1.1)%

Even though total merchandise gross profits have declined primarily from fewer stores, merchandise gross profit per store has consistently improved over prior year results for each of the last twelve quarters.

Merchandise gross profit margins in 1993 increased as a result of the Company's implementation of its everyday-fair-pricing strategy, which reduced discounting and promotional activities (see Management Strategies). Margins have also been favorably affected by lower cigarette costs (beginning in August 1993) and lower product costs under the Company's supply agreement with McLane. In 1994, with the reduction of discounting in place, the Company tested lower prices in certain parts of the country as part of a more aggressive everyday-fair-pricing strategy. These lower prices, combined with increased costs for disposal of slow moving merchandise, was primarily responsible for the decrease in 1994 merchandise margins.

During 1995, merchandise margin declined slightly compared to 1994. While some higher margin categories, such as services, showed good growth throughout the year, overall merchandise margin declined in the fourth quarter almost .5 percent compared to the same period last year. This decline was the result of several factors including rising costs that were not entirely passed on to the consumer, initial introductory costs associated with new fresh-food products and increased focus on deleting slower-moving items. Management is actively working to maintain a merchandise margin level consistent with last year.

Gasoline Gross Profit Data

	Years Ended December 31		
	1995	1994	1993
Gasoline gross profit — *dollars in millions*	$ 192.9	$ 199.6	$ 195.6
Increase/(decrease) from prior year			
Average per store gross profit dollar change	(3.3)%	8.2%	33.4%
Margin point change *(in cents per gallon)*	(.60)	.06	2.37
Average per store gas gallonage	1.0%	7.8%	11.1%

In 1995, gasoline gross profits declined $6.7 million from the levels achieved in 1994 due to lower margins (in cents per gallon), which were affected by market conditions that kept wholesale costs high for much of the year while competitive pressures kept retail prices soft. Gasoline gross profit dollars and margin were unusually high in the fourth quarter of 1994 as a result of favorable market conditions created by the federally mandated fuel reformulation program. Contributing factors to the strong results in 1993, 1994 and the first three quarters of 1995, were the Company's business strategies which closed low-volume locations, enhanced the appeal and convenience of its gas facilities and placed increased emphasis on by-store management of gasoline merchandising.

Operating, Selling, General and Administrative Expenses

(Dollars in Millions)	Years Ended December 31 1995	1994	1993
Total operating, selling, general and administrative expenses	$ 1,867.0	$ 1,888.6	$ 2,030.4
Ratio of reported OSG&A to sales	27.7%	28.3%	30.1%
Decrease in reported OSG&A compared to prior year	$ (21.6)	$ (141.8)	$ (93.7)
Decrease in adjusted OSG&A compared to prior year*	$ (23.9)	$ (86.7)	$ (98.1)

** adjusted to exclude severance and related costs and the loss for store closings and dispositions of properties, including Citijet (see Summary of Results of Operations).*

The majority of the decrease in OSG&A expenses, as adjusted, resulted from cost savings realized from reductions in force that began late in 1992 and continued through 1995, combined with the effect of having

fewer stores (see Management Strategies).

The Company continues to review the functions necessary to enable its stores to respond faster and more cost efficiently to rapidly changing customer needs and preferences. In conjunction with this review, the Company continues to realign and reduce personnel and office facilities, in order to eliminate non-essential costs.

In December 1995, the Company's plans resulted in a $13.4 million accrual, of which $5.0 million was for severance benefits and $8.4 million for reduction of office space. Reductions of more than 400 employees throughout the Company will result in annualized savings of approximately $20 million. The office closings and consolidations involve field operating and staff locations, as well as the Company's headquarters facilities ("Cityplace"). While the execution of the office plans will take most of the year, future years' annualized savings from these initiatives will be approximately $5 million, including potential income from additional Cityplace leases.

In December 1994, the Company accrued $7.4 million for severance costs and office reductions. The employee terminations were completed in 1995, while the office realignments will be completed in 1996 along with those previously discussed. Changes from the estimates for 1994's original $7.4 million accrual did not have a material impact on 1995 earnings.

Interest Expense, Net

The Company's net interest expense in 1995 decreased $9.4 million compared to 1994. Most of the savings related to non-cash interest which declined due to the refinancing of the term loans under the senior bank debt credit agreement ("Credit Agreement") in December 1994 and the extension of the repayment of the debt relating to its headquarters facilities (Cityplace) at a lower interest rate in February 1995 (see Liquidity and Capital Resources — Financing Activities). The adverse impact of the 1.1% rise in the weighted average interest rate on the Company's floating rate debt during 1995 increased interest expense approximately $8 million. However, the 1.5% reduction in the margin that the Company negotiated with its bank lenders in the refinancing in late 1994 offset a portion ($5 million) of this increase.

In November 1995, the Company consummated a $216.7 million tender offer to purchase a portion ($263.3 million face value) of its public debt securities (see Liquidity and Capital Resources — Financing Activities). The purchase was financed by the issuance of $300 million of 4.5% Convertible Quarterly Income Debt Securities due 2010 ("Convertible Debt"). The annual interest expense of $13.7 million from issuing the Convertible Debt will not be offset by a corresponding reduction in interest expense for the retired debentures, since the retired debentures are subject to Statement of Financial Accounting Standards No. 15 ("SFAS No. 15") treatment. Despite the incremental interest expense from the Convertible Debt, the Company expects total interest expense to remain flat in 1996, due to the expectation of lower floating rates and debt balances coupled with lower short-term borrowings from use of the convertible debt proceeds not used in the tender offer.

Net interest expense in 1994 increased $13.2 million over 1993, primarily due to the refinancing of the 12% Senior Notes with working capital and bank debt in August 1993. Unlike the interest on the bank debt, interest on the 12% Senior Notes was subject to SFAS No. 15 treatment with interest payments recorded as a reduction of principal rather than interest expense (see Note 8 of "Notes to Consolidated Financial Statements"). Net interest expense in 1993 was $15.6 million lower than in 1992 primarily due to lower interest rates on floating rate debt, combined with greater use of commercial paper, which has lower interest rates than other debt instruments. Partially offsetting the decline in interest expense was lower interest income resulting from the receipt in 1992 of $5.8 million in interest on tax refunds.

Approximately 35% of the Company's debt contains floating rates, which had a weighted average interest rate of 6.62% for 1995 versus 5.51% and 4.52% for 1994 and 1993, respectively. In the first quarter of 1996, the Company reduced its exposure to short-term fluctuations in rates on a substantial portion of its floating rate bank debt by selecting one year LIBOR maturities at current favorable rates rather than the shorter terms it has selected in the past.

Income Taxes

The Company recorded tax benefits in 1995 and 1994 of $66.1 million and $18.5 million respectively, compared to a tax expense of $8.7 million in 1993. During the fourth quarter of 1994, as a result of the Company's anticipated 1995 taxable earnings, the valuation allowance for deferred taxes was reduced $30 million. During the fourth quarter of 1995, due to the Company's demonstrated ability to produce higher levels of taxable income, the remaining portion of the valuation allowance was reversed producing an $84.3 million benefit.

LIQUIDITY AND CAPITAL RESOURCES

The majority of the Company's working capital is provided from three sources: i) cash flows generated from its operating activities; ii) a $400 million commercial paper facility (guaranteed by Ito-Yokado Co., Ltd.); and iii) short-term seasonal borrowings of up to $150 million under its revolving credit facility. The Company believes that operating activities coupled with available short-term working capital facilities will provide sufficient liquidity to

fund current operating and capital expenditure programs, as well as to service debt requirements.

Financing Activities

On November 22, 1995, the Company completed a tender offer for 40% of the face value of both its 5% First Priority Senior Subordinated Debentures due December 15, 2003 ($180.6 million) and 4½% Second Priority Senior Subordinated Debentures-Series A ($82.7 million) due June 15, 2004 (collectively, the "Debentures"). Under the terms of the offer the final clearing prices were $840.00 and $786.00 for the 5% and 4½% Debentures, respectively, per $1,000 face amount, resulting in a cash outlay by the Company of $216.7 million.

To finance the purchase of the Debentures, the Company issued $300 million in Convertible Debt to Ito-Yokado Co., Ltd., and Seven-Eleven Japan Co., Ltd., the joint owners of IYG Holding Company, which is the Company's majority shareholder. The remaining proceeds of $83.3 million were made available for general corporate purposes. The Convertible Debt is subordinated to all existing debt, has a 15 year term with no amortization and is convertible into the Company's common shares at $4.16 per share.

The Company recognized a $103.2 million after tax extraordinary gain on the purchase of the Debentures in the fourth quarter of 1995. The gain results from purchasing the Debentures below their face value and from retiring the future undiscounted interest payments on that portion of the Debentures being purchased. As a result of the Company's financial restructuring in 1991, SFAS No. 15 required the Company to include its future undiscounted interest payments on the Debentures in the carrying value of the debt on the balance sheet.

The Company's Credit Agreement contains a $300 million term loan and a revolving credit facility. The term loan has scheduled quarterly repayments of $18.75 million commencing March 31, 1996, through December 31, 1999. The revolving credit facility contains both a revolving loan ("Revolver") and letter of credit subfacility, each having a maximum limit of $150 million and expiring on December 31, 1999. Interest on the Revolver and Term Loan is generally based on a variable rate equal to the administrative agent bank's base rate or, at the Company's option, at a rate equal to the Eurodollar rate plus .975% per year.

The Credit Agreement contains certain financial and operating covenants requiring, among other things, the maintenance of certain financial ratios, including interest coverage, fixed charge coverage and senior indebtedness to earnings before interest, taxes, depreciation and amortization ("EBITDA"). The covenant levels established by the Credit Agreement generally require continuing improvement in the Company's financial condition.

For the period ended December 31, 1995, the Company was in compliance with all of the covenants required under the Credit Agreement, including compliance with the principal financial and operating covenants (calculated over the latest 12-month period) as follows:

		Requirements:	
Covenants	**Actuals**	**Minimum**	**Maximum**
Interest coverage*	2.82 to 1.0	2.70 to 1.0	
Fixed charge coverage	1.10 to 1.0	1.00 to 1.0	
Senior indebtedness to EBITDA	3.56 to 1.0		4.10 to 1.0

** includes effects of the SFAS No. 15 interest payments.*

The issuance of the Convertible Debt and the tender offer for the Debentures did not require the approval of the Company's lenders under the Credit Agreement. However, during the fourth quarter, the Company obtained an amendment to the Credit Agreement that allows greater flexibility on uses of the proceeds from the issuance of the Convertible Debt and how the refinancing is treated under certain financial covenants. The amendment allows the Company, among other things, to make subsequent purchases of subordinated debt with any remaining proceeds and to exclude payments for such purchases from the Company's fixed charge coverage ratio.

In 1995, the Company repaid $289.4 million of debt, of which $216.7 million related to the tender offer for the Debentures. Other principal reductions during the year were $72.7 million of which $34.6 million was for SFAS No. 15 interest and $23.9 million was for principal payments on the Company's Yen denominated loan (secured by the royalty income stream from its area licensee in Japan). Outstanding balances at December 31, 1995, for the commercial paper, the Term Loan and the Revolver were $350.2 million, $300.0 million and zero, respectively. As of December 31, 1995, outstanding letters of credit issued pursuant to the Credit Agreement totaled $80.4 million.

As a result of an agreement reached in conjunction with the Company's bankruptcy proceedings in 1990, on February 15, 1995, the 7⅞% Cityplace notes, issued by Cityplace Center East Corporation ("CCEC"), a wholly owned subsidiary of the Company, were repaid under a drawing of a letter of credit issued by The Sanwa Bank, Ltd. Under such agreement, the term of maturity of the indebtedness of CCEC resulting from such draw has been extended by ten years to March 1, 2005. New terms include monthly payments of principal and interest over the ten-year period, based upon a 25-year amortization at 7½%, with the remaining principal due upon maturity.

Cash From Operating Activities

Net cash provided by operating activities was $236.2 million for 1995, compared to $271.6 million in 1994 and $232.1 million in 1993 (see "Results of Operations" section). In 1995, other items affecting operating cash flows included a $13.4 million payment related to an IRS examination of the Company's filings for 1990 and 1991. Such payment had no material effect on 1995 earnings.

Capital Expenditures

During 1995, net cash used in investing activities consisted primarily of payments of $192.2 million for property and equipment, the majority of which was used for remodeling stores, upgrading retail gasoline facilities, replacing equipment and complying with environmental regulations. Through December 31, 1995, approximately 4,100 stores have been remodeled. The remodels are focusing on the features that are most noticeable to customers and have the most immediate and positive impact on store performance, such as lighting and security, food service equipment, necessary maintenance and consistent image.

The Company expects 1996 capital expenditures to be approximately $210 million (excluding lease commitments), primarily to complete remodels started in 1995 and to remodel about 1,100 additional stores. The remaining capital will be used for development of new store sites, to replace equipment, to upgrade gasoline facilities and to comply with environmental regulations. While the Company will look at the economics of each new site, it anticipates that it will finance new store construction primarily through leases containing initial terms of 15-20 years with typical option renewal periods.

Capital Expenditures — Gasoline Equipment

The Company incurs ongoing costs to comply with federal, state and local environmental laws and regulations primarily relating to underground storage tank ("UST") systems. The Company anticipates it will spend approximately $12 million in 1996 on capital improvements required to comply with environmental regulations relating to USTs, as well as above-ground vapor recovery equipment at store locations and approximately an additional $21 million on such capital improvements from 1997 through 1999.

Environmental Compliance — Stores

The Company accrues for the anticipated future costs of environmental clean-up activities (consisting of environmental assessment and remediation) relating to detected releases of regulated substances at its existing and previously owned or operated sites at which gasoline has been sold (including store sites and other facilities that have been sold by the Company). At December 31, 1995, the Company has an accrued liability of $63.7 million for such activities and anticipates that substantially all such expenditures will be incurred within the next five years. This estimate is based on the Company's prior experience with gasoline sites and its consideration of such factors as the age of the tanks, location of tank sites and experience with contractors who perform environmental assessment and remedial work.

Under state reimbursement programs the Company is eligible to receive reimbursement for a portion of future costs, as well as costs previously paid. At December 31, 1995, the Company has recorded a gross receivable of $73.4 million (a net receivable of $59.7 million after an allowance of $13.7 million) for the estimated probable state reimbursement. There is no assurance of the timing of the receipt of state reimbursement funds; however, based on its experience, the Company expects to receive the majority of state reimbursement funds within one to four years after payment of eligible assessment and remediation expenses, assuming that the state administrative procedures for processing such reimbursements have been fully developed.

The estimated future assessment and remediation expenditures and related state reimbursement amounts could change within the near future as governmental requirements and state reimbursement programs continue to be implemented or revised.

Environmental Compliance — Chemical Plant

In December 1988, the Company closed its chemical manufacturing facility in New Jersey. As a result, the Company is required to conduct environmental remediation at the facility and has accrued a liability for this purpose. As required, the Company has submitted a clean-up plan to the New Jersey Department of Environmental Protection (the "State"), which provides for remediation of the site for approximately a three to five year period, as well as continued groundwater treatment for a projected 20 year period. While the Company has received initial comments from the State, the clean-up plan has not been finalized. The Company has recorded liabilities representing its best estimates of the clean-up costs of $37.8 million at December 31, 1995. Of this amount, $31.7 million was included in deferred credits and other liabilities and the remainder in accrued expenses and other liabilities. In 1991, the Company entered into a settlement agreement with a large chemical company that formerly owned the facility. Under the settlement agreement, the former owner agreed to pay a substantial portion of the clean-up costs described above. The Company has recorded a receivable of $22.0 million at December 31, 1995, representing the former owner's portion of the clean-up costs.

None of the amounts related to environmental liabilities have been discounted.

(Dollars in Thousands, Except Per-Share Data)	December 31 1995	December 31 1994
ASSETS		
Current assets:		
Cash and cash equivalents	$ 43,047	$ 59,288
Accounts and notes receivable	107,224	102,230
Inventories	102,020	101,468
Other current assets	103,816	40,411
Total current assets	356,107	303,397
Property and equipment	1,335,783	1,314,499
Other assets	389,227	382,698
	$ 2,081,117	$ 2,000,594
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Trade accounts payable	$ 195,154	$ 203,315
Accrued expenses and other liabilities	329,429	316,183
Commercial paper	50,198	41,322
Long-term debt due within one year	145,346	123,989
Total current liabilities	720,127	684,809
Deferred credits and other liabilities	236,545	245,807
Long-term debt	1,705,237	2,227,209
Convertible quarterly income debt securities	300,000	—
Commitments and contingencies		
Shareholders' equity (deficit):		
Common stock, $.0001 par value; 1,000,000,000 shares authorized; 409,922,935 shares issued and outstanding	41	41
Additional capital	625,574	625,574
Accumulated deficit	(1,506,407)	(1,782,846)
Total shareholders' equity (deficit)	(880,792)	(1,157,231)
	$ 2,081,117	$ 2,000,594

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF EARNINGS

(Dollars in Thousands, Except Per-Share Data)	Years Ended December 31 1995	1994	1993
Revenues:			
Net sales (including $991,788, $992,970 and $962,955 in excise taxes)	$ 6,745,820	$ 6,684,495	$ 6,744,333
Other income	70,969	66,407	61,592
	6,816,789	6,750,902	6,805,925
Costs and expenses:			
Cost of goods sold	4,762,707	4,693,826	4,696,309
Operating, selling, general and administrative expenses	1,866,971	1,888,610	2,030,382
Interest expense, net	85,582	94,970	81,814
	6,715,260	6,677,406	6,808,505
Earnings (loss) before income taxes, extraordinary gain and cumulative effect of accounting change	101,529	73,496	(2,580)
Income taxes (benefit)	(66,065)	(18,500)	8,700
Earnings (loss) before extraordinary gain and cumulative effect of accounting change	167,594	91,996	(11,280)
Extraordinary gain on debt redemption (net of tax effect of $8,603 in 1995 and $0 in 1993)	103,169	—	98,968
Cumulative effect of accounting change for postemployment benefits	—	—	(16,537)
Net earnings	$ 270,763	$ 91,996	$ 71,151
Earnings (loss) per common share (primary and fully diluted):			
Before extraordinary gain and cumulative effect of accounting change	$ .40	$ .22	$ (.03)
Extraordinary gain	.25	—	.24
Cumulative effect of accounting change	—	—	(.04)
Net earnings	$ .65	$ .22	$ .17

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (DEFICIT)

(Dollars in Thousands, Except Share Amounts)	Common Stock Shares	Common Stock Amount	Additional Capital	Accumulated Deficit	Total Shareholders' Equity (Deficit)
Balance, January 1, 1993	410,022,481	$ 41	$ 625,724	$ (1,944,524)	$ (1,318,759)
Net earnings	—	—	—	71,151	71,151
Cancellation of shares	(99,546)	—	(150)	112	(38)
Foreign currency translation adjustments	—	—	—	(704)	(704)
Balance, December 31, 1993	409,922,935	41	625,574	(1,873,965)	(1,248,350)
Net earnings	—	—	—	91,996	91,996
Foreign currency translation adjustments	—	—	—	(877)	(877)
Balance, December 31, 1994	409,922,935	41	625,574	(1,782,846)	(1,157,231)
Net earnings	—	—	—	270,763	270,763
Foreign currency translation adjustments	—	—	—	(2,470)	(2,470)
Other	—	—	—	8,146	8,146
Balance, December 31, 1995	409,922,935	$ 41	$ 625,574	$ (1,506,407)	$ (880,792)

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in Thousands)	1995	1994	1993
	Years Ended December 31		
Cash flows from operating activities:			
Net earnings	$ 270,763	$ 91,996	$ 71,151
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Extraordinary gain on debt redemption	(103,169)	—	(98,968)
Cumulative effect of accounting change for postemployment benefits	—	—	16,537
Depreciation and amortization of property and equipment	147,423	143,670	134,920
Other amortization	19,026	19,026	19,430
Deferred income taxes	(84,269)	(30,000)	—
Noncash interest expense	1,974	11,384	8,497
Other noncash (income) expense	(409)	614	3,393
Net loss on property and equipment	7,274	7,504	36,226
(Increase) decrease in accounts and notes receivable	(2,708)	(3,066)	24,937
(Increase) decrease in inventories	(552)	7,895	16,347
(Increase) decrease in other assets	(1,053)	24,273	3,344
Decrease in trade accounts payable and other liabilities	(18,083)	(1,729)	(3,737)
Net cash provided by operating activities	236,217	271,567	232,077
Cash flows from investing activities:			
Payments for purchase of property and equipment	(192,221)	(171,636)	(195,146)
Proceeds from sale of property and equipment	15,720	15,867	22,809
Other	2,770	2,371	4,982
Net currency exchange principal transactions	—	(5,133)	(8,894)
Cash utilized by distribution and food center assets	—	(2,790)	(17,739)
Proceeds from sale of distribution and food center assets	—	6,305	44,889
Net cash used in investing activities	(173,731)	(155,016)	(149,099)
Cash flows from financing activities:			
Proceeds from commercial paper and revolving credit facilities	4,171,927	4,451,774	4,111,500
Payments under commercial paper and revolving credit facilities	(4,256,918)	(4,418,693)	(3,927,234)
Proceeds from issuance of long-term debt	—	300,000	150,000
Principal payments under long-term debt agreements	(289,372)	(400,580)	(403,125)
Proceeds from issuance of convertible quarterly income debt securities	300,000	—	—
Debt issuance costs	(4,364)	(3,250)	(2,437)
Net cash used in financing activities	(78,727)	(70,749)	(71,296)
Net (decrease) increase in cash and cash equivalents	(16,241)	45,802	11,682
Cash and cash equivalents at beginning of year	59,288	13,486	1,804
Cash and cash equivalents at end of year	$ 43,047	$ 59,288	$ 13,486
Related disclosures for cash flow reporting:			
Interest paid, excluding SFAS No. 15 Interest	$ (97,945)	$ (98,157)	$ (87,631)
Net income taxes paid	$ (34,674)	$ (7,810)	$ (7,969)

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

YEARS ENDED DECEMBER 31, 1995, 1994 AND 1993

1. ACCOUNTING POLICIES

Principles of Consolidation

The Southland Corporation and subsidiaries ("the Company") is owned approximately 64% by IYG Holding Company, which is jointly owned by Ito-Yokado Co., Ltd. ("IY") and Seven-Eleven Japan Co., Ltd. ("SEJ").

The consolidated financial statements include the accounts of The Southland Corporation and its subsidiaries. Intercompany transactions and account balances are eliminated. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from those estimates. Prior-year and quarterly amounts have been reclassified to conform to the current-year presentation. Buying and occupancy expense of $492,499,000 and $513,393,000 for the years ended December 31, 1994 and 1993, respectively, was reclassified from cost of goods sold to operating, selling, general and administrative expenses ("OSG&A").

The Company operates more than 5,400 7-Eleven and other convenience stores in the United States and Canada. Area licensees, or their franchisees, and affiliates operate approximately 10,000 additional 7-Eleven convenience stores in certain areas of the United States, in 18 foreign countries and in the U. S. territories of Guam and Puerto Rico. The Company's net sales are comprised of sales of groceries, take-out foods and beverages, gasoline (at certain locations), dairy products, non-food merchandise, specialty items and services. Net sales and cost of goods sold of stores operated by franchisees are consolidated with the results of Company-operated stores. Net sales of stores operated by franchisees are $2,832,131,000, $2,820,685,000 and $2,810,270,000 from 2,896, 2,962 and 2,998 stores for the years ended December 31, 1995, 1994 and 1993, respectively. Under the present franchise agreements, initial franchise fees are recognized in income currently and are generally calculated based upon gross profit experience for the store or market area. These fees cover certain costs including training, an allowance for travel, meals and lodging for the trainees and other costs relating to the franchising of the store.

The gross profit of the franchise stores is split between the Company and its franchisees. The Company's share of the gross profit of franchise stores is its continuing franchise fee, generally ranging from 50% to 58% of the gross profit of the store, which is charged to the franchisee for the license to use the 7-Eleven operating system and trademarks, for the lease and use of the store premises and equipment, and for continuing services provided by the Company. These services include merchandising, advertising, recordkeeping, store audits, contractual indemnification, business counseling services and preparation of financial statements. The gross profit earned by the Company's franchisees of $515,610,000, $517,955,000 and $530,436,000 for the years ended December 31, 1995, 1994 and 1993, respectively, is included in the Consolidated Statements of Earnings as OSG&A.

Sales by stores operated under domestic and foreign area license agreements are not included in consolidated revenues. All fees or royalties arising from such agreements are included in other income. Initial fees, which have been immaterial, are recognized when the services required under the agreements are performed.

Other Income

Other income is primarily area license royalties and franchise fee income. The area license royalties include amounts from area license agreements with SEJ of approximately $44,000,000, $42,000,000 and $39,000,000 for the years ended December 31, 1995, 1994 and 1993, respectively.

Operating, Selling, General and Administrative Expenses

Buying and occupancy expenses are included in OSG&A.

Interest Expense

Interest expense is net of interest income of $16,975,000, $13,618,000 and $12,745,000 for the years ended December 31, 1995, 1994 and 1993, respectively.

Cash and Cash Equivalents

Cash and cash equivalents include temporary cash investments of $8,787,000 and $3,028,000 at December 31, 1995 and 1994, respectively, stated at cost, which approximates market. The Company considers all highly liquid investment instruments purchased with maturities of three months or less to be cash equivalents.

Inventories

Inventories are stated at the lower of cost or market. Cost is generally determined by the LIFO method for stores in the United States and by the FIFO method for stores in Canada.

Depreciation and Amortization

Depreciation of buildings and equipment is based upon the estimated useful lives of these assets using the straight-line method. Amortization of capital leases, improvements to leased properties and favorable leaseholds is based upon the remaining terms of the leases or the estimated useful lives, whichever is shorter.

Foreign and domestic area license royalty intangibles were recorded in 1987 at the fair value of future royalty payments and are being amortized over 20 years using the straight-line method. The 20-year life is less than the estimated lives of the various royalty agreements, the majority of which are perpetual.

Store Closings

Provision is made on a current basis for the write-down of identified owned-store closings to their net realizable value. For identified leased-store closings, leasehold improvements are written down to their net realizable value and a provision is made on a current basis if anticipated expenses are in excess of expected sublease rental income.

Business Segment

The Company operates in a single business segment — the operating, franchising and licensing of convenience food stores, primarily under the 7-Eleven name.

2. ACCOUNTS AND NOTES RECEIVABLE

(Dollars in Thousands)	December 31 1995	December 31 1994
Notes receivable (net of long-term portion of $14,606 and $15,309)	$ 2,273	$ 5,773
Trade accounts receivable	48,599	42,856
Franchisee accounts receivable	43,556	47,682
Environmental cost reimbursements (net of long-term portion of $64,034 and $67,546) — see Note 13	17,654	12,709
	112,082	109,020
Allowance for doubtful accounts	(4,858)	(6,790)
	$ 107,224	$ 102,230

3. INVENTORIES

Inventories stated on the LIFO basis that are included in inventories in the accompanying Consolidated Balance Sheets were $62,705,000 and $63,340,000 at December 31, 1995 and 1994, respectively, which is less than replacement cost by $30,907,000 and $28,286,000, respectively. At December 31, 1993, inventories were reduced resulting in a liquidation of LIFO inventory layers recorded at costs that were lower than the costs of current purchases. The effect of this reduction was to decrease cost of goods sold by approximately $3,900,000 in 1993.

4. OTHER CURRENT ASSETS

(Dollars in Thousands)	December 31 1995	December 31 1994
Prepaid expenses	$ 17,775	$ 18,474
Deferred tax assets (net of allowance of $77,218 in 1994)	78,665	13,861
Other	7,376	8,076
	$ 103,816	$ 40,411

5. PROPERTY AND EQUIPMENT

(Dollars in Thousands)	December 31 1995	1994
Cost:		
Land	$ 461,585	$ 475,611
Buildings and leaseholds	1,274,651	1,223,128
Equipment	697,673	623,755
Construction in process	32,725	35,634
	2,466,634	2,358,128
Accumulated depreciation and amortization	(1,130,851)	(1,043,629)
	$ 1,335,783	$ 1,314,499

During 1995, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 121, "Accounting for the Impairment of Long-Lived Assets." The statement establishes accounting standards for the impairment of long-lived assets to be held and used and for long-lived assets to be disposed of, and must be adopted no later than 1996. The impact on the Company's earnings is not expected to be material when the Company adopts the statement in 1996.

6. OTHER ASSETS

(Dollars in Thousands)	December 31 1995	1994
Japanese license royalty intangible (net of accumulated amortization of $132,988 and $116,972)	$ 185,513	$ 201,528
Other license royalty intangibles (net of accumulated amortization of $23,750 and $20,914)	32,854	35,690
Environmental cost reimbursements (net of allowance of $13,705 and $18,890) — see Note 13	64,034	67,546
Deferred tax assets (net of allowance of $97,371 in 1994)	30,396	16,139
Other (net of accumulated amortization of $5,023 and $7,281)	76,430	61,795
	$ 389,227	$ 382,698

7. ACCRUED EXPENSES AND OTHER LIABILITIES

(Dollars in Thousands)	December 31 1995	1994
Accrued insurance	$ 83,068	$ 95,372
Accrued payroll	43,025	51,024
Accrued taxes, other than income	40,710	40,372
Accrued environmental costs (see Note 13)	40,659	35,574
Other	121,967	93,841
	$ 329,429	$ 316,183

Other includes accounts payable to The Southland Corporation Employees' Savings and Profit Sharing Plan (see Note 12) for contributions and contingent rent payables of $13,635,000 and $13,186,000 as of December 31, 1995 and 1994, respectively.

The Company continues to review the functions necessary to enable its stores to respond faster, more creatively and more cost efficiently to rapidly changing customer needs and preferences. To accomplish this goal, the Company continues to realign and reduce personnel and office facilities.

In December 1995, the Company accrued $13,415,000 for severance benefits for employees to be terminated and for reduction in office space. The cost of the reorganization plan was recorded in OSG&A and is comprised of $4,979,000 for severance benefits and $8,436,000 for reductions in office facilities.

In December 1994, the Company accrued $7,405,000 for severance benefits for employees terminated and for changes in office facilities. The employee terminations were substantially completed in 1995, and the office realignments are scheduled for completion in 1996. Changes in estimates from the original $7,405,000 accrual did not have a material impact on 1995 earnings.

8. DEBT

(Dollars in Thousands)	December 31 1995	December 31 1994
Bank Debt Term Loans	$ 300,000	$ 300,000
Bank Debt revolving credit facility	—	50,000
Commercial paper	300,000	350,000
5% First Priority Senior Subordinated Debentures due 2003	377,558	615,539
4½% Second Priority Senior Subordinated Debentures (Series A) due 2004	170,952	294,597
4% Second Priority Senior Subordinated Debentures (Series B) due 2004	25,146	25,897
12% Second Priority Senior Subordinated Debentures (Series C) due 2009	57,082	59,696
6¼% Yen Loan	229,243	253,114
7½% Cityplace Term Loan due 2005	286,949	289,598
Canadian revolving credit facility	11,179	5,678
Capital lease obligations	90,852	105,159
Other	1,622	1,820
	1,850,583	2,351,198
Less long-term debt due within one year	145,346	123,989
	$ 1,705,237	$ 2,227,209

Bank Debt

The Company is obligated to a group of lenders under a credit agreement ("Credit Agreement") that includes term loans and a revolving credit facility (collectively "Bank Debt"). In December 1994, the Credit Agreement was amended to extend its maturity through December 31, 1999, and to change various financial and operating covenants to reduce certain restrictions. The financial and operating covenants require, among other things, the maintenance of certain financial ratios including interest coverage, fixed-charge coverage and senior indebtedness to earnings before interest, income taxes, depreciation and amortization. The Credit Agreement also contains various covenants which, among other things, (a) limit the Company's ability to incur or guarantee indebtedness or other liabilities other than under the Credit Agreement, (b) restrict the Company's ability to engage in asset sales and sale/leaseback transactions, (c) restrict the types of investments the Company can make and (d) restrict the Company's ability to pay cash dividends, redeem or prepay principal and interest on any subordinated debt and certain senior debt. Under the Credit Agreement, all of the assets of the Company, with the exception of certain specified property, serve as collateral.

The amendment to the Credit Agreement refinanced the existing term loans and revolving credit facility with a new term loan and a new revolving credit facility. The new term loan provided proceeds of $300 million, which were primarily used to retire the existing term loans. The new term loan is to be repaid in 16 quarterly installments of $18,750,000 commencing March 31, 1996. The new revolving credit facility makes available borrowings and letters of credit totaling a maximum of $300 million. Maximum borrowings and letters of credit under the revolving credit facility are set at $150 million each. Upon expiration of the facility, all the then outstanding letters of credit must expire and may need to be replaced, and all other amounts then outstanding will be due and payable in full. At December 31, 1995, outstanding letters of credit related to the Credit Agreement totaled $80,409,000.

Interest on the Bank Debt is generally payable quarterly and is based on a variable rate equal to the administrative agent bank's base rate or, at the Company's option, at a rate equal to a reserve-adjusted Eurodollar rate plus .975% per year. The weighted-average interest rate on the term loan outstanding at December 31, 1995 and 1994 was 6.9% and 7.1%, respectively. The weighted-average interest rate on revolving credit facility borrowings outstanding at December 31, 1994, was 8.5%. A fee of .925% per year on the outstanding amount of letters of credit is required to be paid quarterly. A .5% per year commitment fee on unadvanced funds, which for purposes of this calculation includes unissued letters of credit, is payable quarterly.

Commercial Paper

The Company has a facility that provides for the issuance of up to $400 million in commercial paper. At December 31, 1995, $300 million of the $350,198,000 outstanding principal, net of discount, was classified as long-term debt since the Company intends to maintain at least this amount outstanding during the next year. Such

debt is unsecured and is fully and unconditionally guaranteed by IY. IY has agreed to continue its guarantee of all commercial paper issued through 1996. While it is not anticipated that IY would be required to perform under its commercial paper guarantee, in the event IY makes any payments under the guarantee, the Company and IY have entered into an agreement by which the Company is required to reimburse IY subject to restrictions in the Credit Agreement. The weighted-average interest rate on commercial paper borrowings outstanding at December 31, 1995 and 1994, respectively, was 5.8% and 6.0%.

Notes and Debentures

The Notes and Debentures are accounted for in accordance with SFAS No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructuring," and were initially recorded at an amount equal to the future undiscounted cash payments, both principal and interest ("SFAS No. 15 Interest"). Accordingly, no interest expense will be recognized over the life of these securities, and cash interest payments will be charged against the recorded amount of such securities. Interest on all of the Notes and Debentures is payable in cash semiannually on June 15 and December 15 of each year.

The 5% First Priority Senior Subordinated Debentures, due December 15, 2003, had an outstanding principal amount of $269,993,000 at December 31, 1995, and are redeemable at any time at the Company's option at 100% of the principal amount.

The Second Priority Senior Subordinated Debentures were issued in three series, and each series is redeemable at any time at the Company's option at 100% of the principal amount and are described as follows:

— 4½% Series A Debentures, due June 15, 2004, with an outstanding principal amount of $123,654,000 at December 31, 1995.

— 4% Series B Debentures, due June 15, 2004, with an outstanding principal amount of $18,766,000 at December 31, 1995.

— 12% Series C Debentures, due June 15, 2009, with an outstanding principal amount of $21,787,000 at December 31, 1995.

In November 1995, the Company purchased $180,621,000 of the principal amount of its First Priority Senior Subordinated Debentures due 2003 ("5% Debentures") and $82,719,000 of the principal amount of its 4½% Second Priority Senior Subordinated Debentures (Series A) due 2004 ("4½% Debentures") (collectively, "Refinanced Debentures") with a portion of the proceeds from the issuance of $300 million principal amount of Convertible Quarterly Income Debt Securities (see Note 9). The purchase of the Refinanced Debentures resulted in an extraordinary gain of $103,169,000 (net of current tax effect of $8,603,000) as a result of the discounted purchase price and the inclusion of SFAS No. 15 Interest in the carrying amount of the debt.

Prior to the refinancing, the 5% Debentures were subject to annual sinking fund requirements of $27,037,000 due each December 15, commencing 1996 through 2002. The Company used its purchase of the 5% Debentures to satisfy such sinking fund requirements in direct order of maturity until December 15, 2002, at which time a sinking fund payment of $8,638,000 will be due.

The Debentures contain certain covenants that, among other things, (a) limit the payment of dividends and certain other restricted payments by both the Company and its subsidiaries, (b) require the purchase by the Company of the Debentures at the option of the holder upon a change of control, (c) limit additional indebtedness, (d) limit future exchange offers, (e) limit the repayment of subordinated indebtedness, (f) require board approval of certain asset sales, (g) limit transactions with certain stockholders and affiliates, and (h) limit consolidations, mergers and the conveyance of all or substantially all of the Company's assets.

The First and Second Priority Senior Subordinated Debentures are subordinate to the outstanding Bank Debt and to previously outstanding mortgages and notes that are either backed by specific collateral or are general unsecured, unsubordinated obligations. The Second Priority Debentures are subordinate to the First Priority Debentures.

The Company had an issuance of 12% Senior Notes, which were redeemed in 1993 resulting in an extraordinary gain of $98,968,000, which had no tax effect.

Yen Loan

In March 1988, the Company monetized its future royalty payments from SEJ, its area licensee in Japan, through a loan that is nonrecourse to the Company as to principal and interest. The original amount of the yen-denominated debt was 41 billion yen (approximately $327,000,000 at the exchange rate in March 1988) and is collateralized by the Japanese trademarks and a pledge of the future royalty payments. By designating its future royalty receipts during the term of the loan to service the monthly interest and principal payments, the Company has hedged the impact of future exchange rate fluctuations. Payment of the debt is required no later than March 2006 through future royalties from the Japanese licensee, and the Company believes it is a remote possibility that there will be any principal balance remaining at that date. Upon the later of February 28, 2000, or the date which is one year following the final repayment of the loan, royalty payments from the area licensee in Japan will be substantially reduced in accordance with the terms of the license agreement. The current interest rate of 6¼% will be reset after March 1998.

Cityplace Debt

Cityplace Center East Corporation ("CCEC"), a subsidiary of the Company, issued $290 million of notes in 1987 to finance the construction of the headquarters tower, a parking garage and related facilities of the Cityplace Center development. The interest rate on these notes was 7⅞%, payable semiannually on February 15 and August 15, and the principal amount was due on February 15, 1995. Because of the application of purchase accounting in 1987, the effective interest rate was 9.0%. The principal amount was paid to noteholders on February 15, 1995, by drawings under letters of credit issued by The Sanwa Bank, Limited, Dallas Agency ("Sanwa"), which has a lien on the property financed. At that time, the Company deferred the maturity of the debt by exercising its option of extending the term of maturity ten years to March 1, 2005, with monthly payments of principal and interest to Sanwa based on a 25-year amortization at 7½%, with the remaining principal due upon maturity (the "Cityplace Term Loan").

The Company is occupying part of the building as its corporate headquarters and the balance is subleased. As additional consideration through the extended term of the debt, CCEC will pay to Sanwa an amount that it receives from the Company which is equal to the net sublease income that the Company receives on the property and 60% of the proceeds, less $275 million and permitted costs, upon a sale or refinancing of the building.

Southland Canada Debt

In November 1995, Southland Canada, Inc., entered into a revolving credit facility with a Canadian chartered bank, which replaces a similar facility established in 1988. The facility provides bank financing of up to Canadian $15 million (approximately U.S. $10,994,000 at December 31, 1995) until December 31, 1999, when the facility will expire, and all amounts outstanding will be due and payable in full. At December 31, 1995, the Company was fully drawn under this facility. Interest on such facility is generally payable monthly and is based upon the Canadian Prime rate (7.5% at December 31, 1995) plus .25% per year or a bankers' acceptance rate plus 1.25% per year. The weighted-average interest rate on revolving credit facility borrowings outstanding at December 31, 1995 and 1994, respectively, was 7.5% and 7.3%.

The previous revolving credit facility with the same Canadian chartered bank provided financing in which the maximum amount available declined each year until the facility was scheduled to expire on June 30, 1998. At such time, all amounts outstanding were then due and payable in full. Interest payment terms on this facility were similar to those of the new facility, but interest rates were slightly less favorable.

Maturities

Long-term debt maturities assume the continuance of the commercial paper program. The maturities, which include capital lease obligations and sinking fund requirements, as well as SFAS No. 15 Interest accounted for in the recorded amount of the Debentures, are as follows (dollars in thousands):

1996	$ 145,346
1997	144,164
1998	147,855
1999	158,238
2000	81,654
Thereafter	1,173,326
	$ 1,850,583

9. CONVERTIBLE QUARTERLY INCOME DEBT SECURITIES DUE 2010

In November 1995, the Company issued $300 million principal amount of Convertible Quarterly Income Debt Securities due 2010 ("Convertible Debt") to IY and SEJ. The Company used $216,739,000 of the proceeds to purchase the Refinanced Debentures (see Note 8), and the remaining proceeds were designated for general corporate purposes. The Convertible Debt has an interest rate of 4½% and gives the Company the right to defer interest payments thereon for up to 20 consecutive quarters. The holder of the Convertible Debt can convert it into a maximum of 72,112,000 shares of the Company's common shares. The conversion rate represents a premium to the market value of Southland's common stock at the time of issuance of the Convertible Debt. As of December 31, 1995, no shares had been issued as a result of debt conversion. The Convertible Debt is subordinate to all existing debt.

In addition to the principal amount of the Convertible Debt, the 1995 financial statements include interest payable of $638,000 and interest expense of $1,313,000 related to the Convertible Debt.

10. PREFERRED STOCK

The Company has 5,000,000 shares of preferred stock authorized for issuance. Any preferred stock issued will have such rights, powers and preferences as determined by the Company's Board of Directors.

11. DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The disclosure of the estimated fair value of financial instruments has been determined by the Company using available market information and appropriate valuation methodologies as indicated below.

The carrying amounts of cash and cash equivalents, trade accounts receivable, trade accounts payable and accrued expenses and other liabilities are reasonable estimates of their fair values. Letters of credit are included in the estimated fair value of accrued expenses and other liabilities.

The carrying amounts and estimated fair values of other financial instruments at December 31, 1995, are listed in the following table:

(Dollars in Thousands)	Carrying Amount	Estimated Fair Value
Bank Debt	$ 300,000	$ 300,000
Commercial Paper	350,198	350,198
Debentures	630,738	358,267
Yen Loan	229,243	294,565
Cityplace Term Loan	286,949	304,504
Convertible Debt	300,000	301,530

The methods and assumptions used in estimating the fair value for each of the classes of financial instruments presented in the table above are as follows:

— The carrying amount of the Bank Debt approximates fair value because the interest rates are variable.

— Commercial paper borrowings are sold at market interest rates and have an average remaining maturity of less than 40 days. Therefore, the carrying amount of commercial paper is a reasonable estimate of its fair value. The guarantee of the commercial paper by IY is an integral part of the estimated fair value of the commercial paper borrowings.

— The fair value of the Debentures is estimated based on December 31, 1995, bid prices obtained from investment banking firms where traders regularly make a market for these financial instruments. The carrying amount of the Debentures includes $196,538,000 of SFAS No. 15 Interest.

— The fair value of the Yen Loan is estimated by calculating the present value of the future yen cash flows at current interest and exchange rates.

— The fair value of the Cityplace Term Loan is estimated by calculating the present value of the future cash flows at current interest rates.

— The fair value of the Convertible Debt at December 31, 1995, is estimated by an investment banking firm and includes both an interest rate and an equity component.

12. EMPLOYEE BENEFIT PLANS

Profit Sharing Plans

The Company maintains profit sharing plans for its U.S. and Canadian employees. In 1949, the Company excluding its Canadian subsidiary ("Southland") adopted The Southland Corporation Employees' Savings and Profit Sharing Plan (the "Savings and Profit Sharing Plan") and, in 1970, the Company's Canadian subsidiary adopted the Southland Canada, Inc. Profit Sharing Pension Plan. These plans provide retirement benefits to eligible employees.

Contributions to the Savings and Profit Sharing Plan, a 401(k) defined contribution plan, are made by both the participants and Southland. Southland contributes the greater of approximately 10% of its net earnings or an amount determined by Southland's president. Net earnings as amended during 1995 is calculated without regard to the contribution to the Savings and Profit Sharing Plan, federal income taxes, gains from debt repurchases and refinancings and, at the discretion of Southland's president, income from accounting changes. The contribution by Southland is generally allocated to the participants on the basis of their individual contribution, years of participation in the Savings and Profit Sharing Plan and age. The provisions of the Southland Canada, Inc. Profit Sharing Pension Plan are similar to those of the Savings and Profit Sharing Plan. Total contributions to these plans for the years ended December 31, 1995, 1994 and 1993 were $11,318,000, $10,513,000 and $11,956,000 (including amounts allocated to the distribution and food centers in 1994 and 1993), respectively, and are included in OSG&A.

Postretirement Benefits

The Company's group insurance plan (the "Insurance Plan") provides postretirement medical and dental benefits for all retirees that meet certain criteria. Such criteria include continuous participation in the Insurance Plan ranging from 10 to 15 years depending on hire date, and the sum of age plus years of continuous service equal to at least 70. The Company contributes toward the cost of the Insurance Plan a fixed dollar amount per retiree based on age and number of dependents covered, as adjusted for actual claims experience. All other future costs and cost increases will be paid by the retirees. The Company continues to fund its cost on a cash basis; therefore, no plan assets have been accumulated.

Net periodic postretirement benefit costs for 1995, 1994 and 1993 include the following components:

(Dollars in Thousands)	1995	1994	1993
Service cost	$ 585	$ 752	$ 824
Interest cost	1,678	1,732	2,048
Amortization of unrecognized gain	(583)	(61)	—
	$ 1,680	$ 2,423	$ 2,872

The weighted-average discount rate used in determining the accumulated postretirement benefit obligation was 7% and 8% at December 31, 1995 and 1994, respectively. Components of the accrual recorded in the Company's consolidated balance sheets are as follows:

	December 31	
(Dollars in Thousands)	1995	1994
Accumulated Postretirement Benefit Obligation:		
Retirees	$ 11,960	$ 11,197
Active employees eligible to retire	5,234	4,716
Other active employees	6,328	5,354
	23,522	21,267
Unrecognized gains	5,198	7,953
	$ 28,720	$ 29,220

Postemployment Benefits

The Company adopted SFAS No. 112, "Employers' Accounting for Postemployment Benefits," in 1993 and recorded an accumulated postemployment benefit obligation of $16,537,000. The obligation primarily represents future medical costs relating to short-term and long-term disability. The accumulated postemployment benefit obligation, which had no tax effect, was recorded as the cumulative effect of an accounting change. As of December 31, 1995 and 1994, the amount of the obligation was $19,390,000 and $18,460,000, respectively.

Equity Participation Plan

In 1988, the Company adopted The Southland Corporation Equity Participation Plan (the "Participation Plan"), which provides for the granting of both incentive options and nonstatutory options and the sale of convertible

debentures to certain key employees and officers of the Company. In the aggregate, not more than 3,529,412 shares of common stock of the Company can be issued pursuant to the Participation Plan; however, the Company has no present intent to grant additional options or debentures under this plan. The shares available for issuance under the Participation Plan are reduced by the number of shares issued under the Grant Stock Plan, which is described in a following paragraph.

Options were granted in 1988 at the fair market value on the date of grant, which is the same as the conversion price provided in the debentures. All options and convertible debentures that were vested became exercisable as of December 31, 1994, pursuant to the terms of the Participation Plan. At December 31, 1995, there were vested options outstanding to acquire 948,499 shares, of which 909,999 were at $7.50 per share and 38,500 were at $7.70 per share, and vested debentures outstanding that were convertible at $7.50 per share into 5,000 shares. During 1995, options to acquire 812,304 shares and debentures convertible into 12,833 shares expired for those participants who are no longer with the Company. All options expire, and the debentures mature, no later than December 31, 1997.

Grant Stock Plan

In 1988, the Company adopted The Southland Corporation Grant Stock Plan (the "Stock Plan"). Under the provisions of the Stock Plan, up to 750,000 shares of common stock are authorized to be issued to certain key employees and officers of the Company. Shares issued under the Stock Plan decrease the number of shares that can be issued pursuant to the Participation Plan. The stock is fully vested upon the date of issuance. As of December 31, 1995, 480,844 shares had been issued pursuant to the Stock Plan. No shares have been issued since 1988, and the Company has no present intent to grant additional shares.

Stock Incentive Plan

The Company adopted The Southland Corporation 1995 Stock Incentive Plan (the "Stock Incentive Plan") in October 1995, subject to shareholder approval, which is being sought at the annual meeting of shareholders to be held in April 1996. The Stock Incentive Plan provides for the granting of stock options, stock appreciation rights, performance shares, restricted stock, restricted stock units, bonus stock and other forms of stock-based awards and authorizes the issuance of up to 41 million shares over a ten-year period. In October 1995, 3,863,600 options were granted, which remain outstanding at December 31, 1995, at the fair market value of $3.1875 per share on the date of grant to certain key employees and officers of the Company. The options granted in 1995 are exercisable in five equal installments beginning one year after grant date with possible acceleration thereafter based upon certain improvements in the stock price of a share of Southland's common stock.

During 1995, the Financial Accounting Standards Board issued SFAS No. 123, "Accounting for Stock-Based Compensation." The statement must be adopted no later than 1996. The Company intends to adopt the disclosure-only requirements of SFAS No. 123 and will therefore continue to apply the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees."

13. LEASES, COMMITMENTS AND CONTINGENCIES

Leases

Certain property and equipment used in the Company's business is leased. Generally, real estate leases are for primary terms from 14 to 20 years with options to renew for additional periods, and equipment leases are for terms from one to ten years. The leases do not contain restrictions that have a material effect on the Company's operations.

The composition of capital leases reflected as property and equipment in the consolidated balance sheets is as follows:

	December 31	
(Dollars in Thousands)	1995	1994
Buildings	$ 116,412	$ 125,600
Equipment	225	225
	116,637	125,825
Accumulated amortization	(77,428)	(78,103)
	$ 39,209	$ 47,722

The present value of future minimum lease payments for capital lease obligations is reflected in the consolidated balance sheets as long-term debt. The amount representing imputed interest necessary to reduce net minimum lease payments to present value has been calculated generally at the Company's incremental borrowing rate at the inception of each lease.

Future minimum lease payments for years ending December 31 are as follows:

(Dollars in Thousands)	Capital Leases	Operating Leases
1996	$ 21,965	$ 116,621
1997	20,424	105,284
1998	18,793	85,471
1999	17,449	64,869
2000	15,485	48,704
Thereafter	60,405	185,645
Future minimum lease payments	154,521	$ 606,594
Estimated executory costs	(399)	
Amount representing imputed interest	(63,270)	
Present value of future minimum lease payments	$ 90,852	

Minimum noncancelable sublease rental income to be received in the future, which is not included above as an offset to future payments, totals $23,126,000 for capital leases and $21,695,000 for operating leases.

Rent expense on operating leases for the years ended December 31, 1995, 1994 and 1993, totaled $125,456,000, $120,850,000 and $124,402,000, respectively, including contingent rent expense of $8,508,000, $8,576,000 and $8,214,000, but reduced by sublease rent income of $7,296,000, $7,858,000 and $8,545,000. Contingent rent expense on capital leases for the years ended December 31, 1995, 1994 and 1993, was $2,399,000, $2,822,000 and $3,084,000, respectively. Contingent rent expense is generally based on sales levels or changes in the Consumer Price Index.

Leases With The Savings and Profit Sharing Plan

At December 31, 1995, the Savings and Profit Sharing Plan owned 197 stores leased to the Company under capital leases and 634 stores leased to the Company under operating leases at rentals which, in the opinion of management, approximated market rates at the date of lease. In addition, 67, 43 and 62 properties were sold by the Savings and Profit Sharing Plan to third parties in 1995, 1994 and 1993, respectively, and at the same time, the related leases with the Company were either cancelled or assigned to the new owner. Included in the consolidated financial statements are the following amounts related to leases with the Savings and Profit Sharing Plan:

(Dollars in Thousands)	December 31 1995	1994
Buildings (net of accumulated amortization of $8,853 and $9,619)	$ 2,041	$ 3,191
Capital lease obligations (net of current portion of $1,664 and $1,945)	$ 2,310	$ 4,109

(Dollars in Thousands)	Years Ended December 31 1995	1994	1993
Rent expense under operating leases and amortization of capital lease assets	$ 26,850	$ 28,195	$ 30,028
Imputed interest expense on capital lease obligations	$ 483	$ 696	$ 948
Capital lease principal payments included in principal payments under long-term debt agreements	$ 1,818	$ 2,075	$ 2,200

Commitments

McLane Company, Inc.

In connection with the 1992 sale of distribution and food center assets to McLane, the Company and McLane entered into a ten-year service agreement under which McLane is making its distribution services available to 7-Eleven stores in the United States. If the Company does not fulfill its obligation to McLane during this time

period, the Company must reimburse McLane on a pro-rata basis for the transitional payment received at the time of the transaction. The original payment received of $9,450,000 in 1992 is being amortized to cost of goods sold over the life of the agreement. The Company has exceeded the minimum annual purchases each year and expects to exceed the minimum required purchase levels in future years.

Citgo Petroleum Corporation

In 1986, the Company entered into a 20-year product purchase agreement with Citgo to buy specified quantities of gasoline at market prices. These prices are determined pursuant to a formula based on the prices posted by gasoline wholesalers in the various market areas where the Company purchases gasoline from Citgo. Minimum required annual purchases under this agreement are generally the lesser of 750 million gallons or 35% of gasoline purchased by the Company for retail sale. The Company has exceeded the minimum required annual purchases each year and expects to exceed the minimum required annual purchase levels in future years.

Contingencies

Gasoline Store Sites

The Company accrues future costs, as well as records the related probable state reimbursement amounts, for remediation of gasoline store sites where releases of regulated substances have been detected. At December 31, 1995 and 1994, respectively, the Company's estimated liability for sites where releases have been detected was $63,669,000 and $63,424,000, of which $29,174,000 and $32,924,000 are included in deferred credits and other liabilities and the remainder in accrued expenses and other liabilities. The Company has recorded receivables of $59,652,000 and $57,246,000 (net of allowances of $13,705,000 and $18,890,000) for the estimated probable state reimbursements, of which $45,653,000 and $47,746,000 are included in other assets and the remainder in accounts and notes receivable. The Company reduced the estimated net environmental cost reimbursements at the end of 1994 by approximately $6,000,000 as a result of completing a review of state reimbursement programs. The estimated future remediation expenditures and related state reimbursement amounts could change within the near future as governmental requirements and state reimbursement programs continue to be implemented or revised.

The Company anticipates that substantially all of the future remediation costs for sites with detected releases of regulated substances at December 31, 1995, will be incurred within the next five years. There is no assurance of the timing of the receipt of state reimbursement funds. However, based on the Company's experience, the Company expects to receive the majority of state reimbursement funds within one to four years after payment of eligible remediation expenses, assuming that the state administrative procedures for processing such reimbursements have been fully developed.

Chemical Manufacturing Facility

In December 1988, the Company closed its chemical manufacturing facility in New Jersey. As a result, the Company is required to conduct environmental remediation at the facility and has accrued a liability for this purpose. As required, the Company has submitted a clean-up plan to the New Jersey Department of Environmental Protection (the "State"), which provides for remediation of the site for approximately a three-to-five-year period as well as continued groundwater treatment for a projected 20-year period. While the Company has received initial comments from the State, the clean-up plan has not been finalized. The Company has recorded liabilities representing its best estimates of the clean-up costs of $37,824,000 and $39,254,000 at December 31, 1995 and 1994, respectively. Of this amount, $31,660,000 and $34,180,000 are included in deferred credits and other liabilities and the remainder in accrued expenses and other liabilities for the respective years.

The closed chemical manufacturing facility was previously owned by a large chemical company. In 1991, the Company and the former owner executed a final settlement agreement pursuant to which the former owner agreed to pay a substantial portion of the clean-up costs. The Company has recorded receivables of $22,035,000 and $23,009,000 at December 31, 1995 and 1994, respectively, representing the former owner's portion of the clean-up costs. Of this amount, $18,381,000 and $19,800,000 are included in other assets and the remainder in accounts and notes receivable for 1995 and 1994, respectively.

14. INCOME TAXES

As of January 1, 1993, the Company adopted SFAS No. 109, "Accounting for Income Taxes." There was no cumulative effect adjustment upon adoption, and there was no effect on net earnings for the year ended December 31, 1993.

SFAS No. 109 requires the use of the liability method, in which deferred tax assets and liabilities are recognized for differences between the tax basis of assets and liabilities and their reported amounts in the financial statements. Deferred tax assets include tax carryforwards and are reduced by a valuation allowance if, based on available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The components of earnings (loss) before income taxes, extraordinary gain and cumulative effect of accounting change are as follows:

(Dollars in Thousands)	Years Ended December 31 1995	1994	1993
Domestic	$ 98,775	$ 70,615	$ 3,795
Foreign	2,754	2,881	(6,375)
	$ 101,529	$ 73,496	$ (2,580)

The provision for income taxes in the accompanying Consolidated Statements of Earnings consists of the following:

(Dollars in Thousands)	Years Ended December 31 1995	1994	1993
Current:			
Federal	$ 8,251	$ 6,799	$ 2,759
Foreign	8,968	8,515	5,941
State	985	350	—
Tax benefit of operating loss carryforward	—	(4,164)	—
Subtotal	18,204	11,500	8,700
Deferred:			
Provision	60,709	—	—
Beginning of year valuation allowance adjustment	(144,978)	(30,000)	—
Subtotal	(84,269)	(30,000)	—
Income taxes before extraordinary gain and cumulative effect of accounting change	$ (66,065)	$ (18,500)	$ 8,700

Included in Shareholders' Equity at December 31, 1995, is $5,208,000 of income taxes provided in 1995 on an unrealized gain on marketable securities.

Reconciliations of income taxes before extraordinary gain and cumulative effect of accounting change at the federal statutory rate to the Company's actual income taxes provided are as follows:

(Dollars in Thousands)	Years Ended December 31 1995	1994	1993
Taxes (benefit) at federal statutory rate	$ 35,535	$ 25,724	$ (903)
State income taxes, net of federal income tax benefit	640	228	—
Foreign tax rate difference	886	1,212	2,232
Net change in valuation allowance excluding the tax effect of extraordinary items and the cumulative effect of accounting changes	(108,632)	(47,943)	4,112
Other	5,506	2,279	3,259
	$ (66,065)	$ (18,500)	$ 8,700

The valuation allowance for deferred tax assets decreased in 1995 by $174,589,000. The decrease consisted of a $90,320,000 decrease resulting from changes in the Company's gross deferred tax assets and liabilities and an $84,269,000 decrease resulting from a change in estimate regarding the realizability of the Company's deferred tax assets. Based on the Company's trend of positive earnings during the past three years and future expectations, the Company determined that it is more likely than not that its deferred tax assets will be fully realized. In 1994, the valuation allowance decreased by $42,078,000 due to changes in the Company's gross deferred tax assets and liabilities and the realization of $30,000,000 of the Company's net deferred tax asset.

Significant components of the Company's deferred tax assets and liabilities at December 31, 1995 and 1994, are as follows:

(Dollars in Thousands)	Years Ended December 31 1995	1994
Deferred tax assets:		
SFAS No. 15 interest	$ 81,038	$ 125,694
Accrued insurance	55,497	58,514
Accrued liabilities	39,665	43,890
Compensation and benefits	32,365	34,029
Tax credit carryforwards	14,833	48,765
Debt issuance costs	6,820	15,445
Other	5,561	6,172
Subtotal	235,779	332,509
Deferred tax liabilities:		
Area license agreements	(85,164)	(92,515)
Property and equipment	(32,853)	(29,192)
Other	(8,701)	(6,213)
Subtotal	(126,718)	(127,920)
Valuation allowance	—	(174,589)
Net deferred taxes	$ 109,061	$ 30,000

The Company's net deferred tax asset is recorded in other current assets and other assets (see Notes 4 and 6).

At December 31, 1995, the Company had approximately $2,849,000 of general business credit carryforwards and $11,984,000 of alternative minimum tax ("AMT") credit carryforwards. The AMT credits have no expiration date. The general business credits expire during the period from 2007 to 2010.

15. EARNINGS (LOSS) PER COMMON SHARE

Primary earnings (loss) per common share is computed by dividing net earnings, plus Convertible Debt interest (see Note 9) net of tax benefits, by the weighted average number of common shares and common share equivalents outstanding during each year. The exercise of outstanding stock options would not result in a dilution of earnings per share.

16. QUARTERLY FINANCIAL DATA (UNAUDITED)

Summarized quarterly financial data for 1995 and 1994 as adjusted for reclassifications to conform to the current-year presentation (see Note 1) is as follows:

Year Ended December 31, 1995:

(Dollars in Millions, Except Per-Share Data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Net sales	$ 1,545	$ 1,750	$ 1,826	$ 1,625	$ 6,746
Gross profit	449	512	554	468	1,983
Income taxes (benefit)	2	9	12	(89)	(66)
Earnings (loss) before extraordinary gain	(1)	37	50	82	168
Net earnings (loss)	(1)	37	50	185	271
Primary and fully diluted earnings (loss) per common share before extraordinary gain	—	.09	.12	.19	.40

The second quarter includes a $4,679,000 environmental reimbursement related to outstanding litigation. The fourth quarter includes a $103,169,000 extraordinary gain on redemption of debt related to the refinancing of certain debt securities (see Note 8), $84,269,000 from realization of a deferred tax asset (see Note 14) and $13,415,000 of expenses accrued for severance and related costs (see Note 7).

Year Ended December 31, 1994:

(Dollars in Millions, Except Per-Share Data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Net sales	$ 1,512	$ 1,720	$ 1,811	$ 1,641	$ 6,684
Gross profit	442	513	544	492	1,991
Income taxes (benefit)	1	6	6	(32)	(19)
Net earnings (loss)	(8)	32	43	25	92
Primary and fully diluted earnings (loss) per common share	(.02)	.08	.10	.06	.22

The second quarter includes a $4,500,000 recovery on a 1992 insurance claim. The fourth quarter includes $30 million from realization of a deferred tax asset (see Note 14), $7,405,000 of expenses accrued for severance and related costs (see Note 7), $7,696,000 of expense related to store closings and dispositions of properties, and approximately $6,000,000 in expense relating to the reduction of estimated net environmental cost reimbursements (see Note 13).

Independent Auditors' Report

To the Board of Directors and Shareholders of
The Southland Corporation
Dallas, Texas

We have audited the accompanying consolidated balance sheets of The Southland Corporation and Subsidiaries as of December 31, 1995 and 1994, and the related consolidated statements of earnings, shareholders' equity (deficit) and cash flows for each of the three years in the period ended December 31, 1995. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Southland Corporation and Subsidiaries as of December 31, 1995 and 1994, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 1995 in conformity with generally accepted accounting principles.

As discussed in Notes 12 and 14 to the financial statements, in 1993 the Company changed its method of accounting for postemployment benefits and for income taxes to conform with Statements of Financial Accounting Standards No. 112 and No. 109, respectively.

Coopers & Lybrand L.L.P.

Dallas, Texas
February 14, 1996

Directors

MASATOSHI ITO
Chairman of the Board;
Director, Honorary Chairman,
Ito-Yokado Group

TOSHIFUMI SUZUKI (1)
Vice Chairman of the Board;
President and Chief Executive Officer,
Ito-Yokado Co., Ltd.;
Chairman and Chief Executive Officer,
Seven-Eleven Japan Co., Ltd.

JOHN P. THOMPSON (2)
Co-Vice Chairman of the Board;
formerly Chairman,
The Southland Corporation

JERE W. THOMPSON (2)
Co-Vice Chairman of the Board;
formerly President and
Chief Executive Officer,
The Southland Corporation

CLARK J. MATTHEWS, II
President and
Chief Executive Officer;
Secretary,
The Southland Corporation

YOSHITAMI ARAI
Chairman of the Board,
Systems International Incorporated

TIMOTHY ASHIDA (1)
President,
A.K.K. Associates, Inc.

JAY W. CHAI (3)
Chairman of the Board and
Chief Executive Officer,
ITOCHU International Inc.

GARY J. FERNANDES (1) (3)
Senior Vice President and
Director, Electronic Data
Systems Corporation

MASAAKI KAMATA
Executive Vice President,
Seven-Eleven Japan Co., Ltd.

KAZUO OTSUKA (1)
General Manager,
Corporate Development,
Ito-Yokado Co., Ltd.

ASHER O. PACHOLDER (3)
Chairman of the Board
and Chief Financial Officer,
ICO, Inc.

NOBUTAKE SATO
Executive Vice President,
Corporate Planning,
Ito-Yokado Co., Ltd.

TATSUHIRO SEKINE (3)
Senior Managing Director,
Finance,
Ito-Yokado Co., Ltd.

(1) Compensation and Benefits Committee
(2) Retiring as of April 24, 1996
(3) Audit Committee

Officers

MASATOSHI ITO
Chairman of the Board

TOSHIFUMI SUZUKI
Vice Chairman of the Board

CLARK J. MATTHEWS, II
President,
Chief Executive Officer
and Secretary

STEPHEN B. KRUMHOLZ
Executive Vice President
and Chief Operating Officer

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Distribution

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Finance

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Northwest Division

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Vice President,
Southwest Division

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JAMES NOTARNICOLA
Vice President,
Communications

GARY R. ROSE
Vice President,
Gasoline & Environmental Services

DONALD E. THOMAS
Controller

DAVID A. URBEL
Vice President, Planning
and Treasurer

CORPORATE HEADQUARTERS

The Southland Corporation
2711 North Haskell Ave.
Dallas, TX 75204-2906
(214) 828-7011

Mailing Address:
P.O. Box 711
Dallas, TX 75221-0711

FORM 10-K AND OTHER INVESTOR INFORMATION

Requests for the Form 10-K for the year ended December 31, 1995, and quarterly financial information should be addressed to the Investor Relations Manager at the above address, or telephone (214) 828-7328.

Annual reports are mailed to all shareholders. Investors may receive quarterly information regularly by requesting to be included on the company's mailing list.

A recorded company update can be reached and requests for information can be left 24 hours a day by calling (214) 828-7587.

ANNUAL MEETING

The annual meeting will be held at 9:30 a.m. CDT on Wednesday, April 24, 1996, in the Cityplace Conference Center at the company's headquarters. All shareholders and bondholders are cordially invited to attend.

AUDITORS

Coopers & Lybrand L.L.P.
Dallas, Texas

COMMON STOCK

Southland's common stock is traded on The Nasdaq Stock Market under the ticker symbol SLCM. There were 3,097 shareholders of record as of March 8, 1996.

The company has paid no dividends on its common equity as such payments are restricted by the indentures governing its outstanding securities and by Southland's Credit Agreement with its senior lenders.

The table below sets forth the high, low and closing market prices for the periods indicated as provided by Nasdaq.

	PRICE RANGE		
QUARTERS	HIGH	LOW	CLOSE
1995			
FIRST	\$ 4 23/32	\$ 3 7/16	\$ 3 3/4
SECOND	4 3/8	3 7/16	3 7/16
THIRD	4 1/8	2 7/8	3
FOURTH	4 1/4	2 15/16	3 5/16
1994			
FIRST	\$ 6 3/4	\$ 3 13/16	\$ 3 7/8
SECOND	6 1/4	3 7/8	6 1/4
THIRD	6 3/8	4 1/2	5 3/4
FOURTH	5 13/16	4 1/4	4 1/2

COMMON STOCK TRANSFER AGENT/REGISTRAR

Society National Bank
c/o KeyCorp Shareholder Services, Inc.
1201 Elm Street, Suite 5050
Dallas, Texas 75270

OTHER SECURITIES

The following other Southland securities are traded over the counter, and price information is available by calling the company's recorded message at (214) 828-7587:

5% First Priority Senior Subordinated Debentures

Trustee: Society National Bank
Corporate Trust Division
127 Public Square, 15th Floor
Cleveland, OH 44115

4½% Second Priority Senior Subordinated Debentures (Series A)
4% Second Priority Senior Subordinated Debentures (Series B)
12% Second Priority Senior Subordinated Debentures (Series C)

Trustee: The Riggs National Bank of Washington, D.C.
808 17th Street, Northwest, 11th Floor
Washington, DC 20006

7-Eleven Around the World

UNITED STATES

Franchised	2,896 (1)
Company-operated	2,077

CANADA

Company-operated	451 (1)
	5,424

LICENSED OR OPERATED BY AFFILIATES (2)

Japan (3)	6,269
Taiwan	1,158
United States	625
Thailand	554
Hong Kong	328
Mexico	221
Australia	153
South Korea	110
Malaysia	93
Spain	89
Philippines	83
Singapore	77
United Kingdom	53
Norway	39
Sweden	31
China	22
Brazil	14
Puerto Rico	12
Denmark	11
Guam	10
Turkey	9
	9,961
	15,385

(1) The number of franchised stores includes 2 locations in New York in which Southland has no real estate interest. The number of company-operated stores in Canada includes 17 locations in which Southland has no real estate interest.

(2) Sales from stores operated by licensees or affiliates are not included in Southland's "Net Sales." Royalties from licensees are included in "Other Income."

(3) The 7-Eleven licensee in Japan, Seven-Eleven Japan Co., Ltd., and its parent company, Ito-Yokado Co., Ltd., jointly own IYG Holding Company, which owns approximately 64% of Southland's common stock.

STATE/ PROVINCE	7-ELEVEN STORES	OTHER RETAIL	TOTAL
UNITED STATES:			
Arizona	96	0	96
California	1,173	3	1,176
Colorado	241	0	241
Connecticut	38	0	38
Delaware	27	0	27
District of Columbia	18	0	18
Florida	411	0	411
Idaho	14	0	14
Illinois	137	9	146
Indiana	16	4	20
Kansas	17	0	17
Maryland	310	11	321
Massachusetts	34	2	36
Michigan	98	0	98
Missouri	82	2	84
Nevada	187	0	187
New Hampshire	8	3	11
New Jersey	203	0	203
New York	219	0	219
North Carolina	7	0	7
Ohio	15	0	15
Oregon	134	0	134
Pennsylvania	164	3	167
Rhode Island	8	0	8
Texas	286	2	288
Utah	113	0	113
Virginia	601	8	609
Washington	231	0	231
West Virginia	22	1	23
Wisconsin	0	15	15
CANADA:			
Alberta	117	0	117
British Columbia	136	0	136
Manitoba	50	0	50
Ontario	111	0	111
Saskatchewan	37	0	37
TOTAL	5,361	63	5,424

All numbers as of December 31, 1995

THE SOUTHLAND CORPORATION

2711 North Haskell Avenue
Dallas, Texas 75204-2906
Phone: (214) 828-7011

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